FINAL STATEMENT OF REASONS

a) Specific Purpose of the Regulations and Factual Basis for Determination that Regulations Are Necessary

Post Hearing Modification

Section 11-400f.(4)

Specific Purpose:

The definition of a financial audit is being amended to include an audit of the cost data of the non-profit corporation.

Factual Basis:

This amendment is necessary for clarity and consistency with Welfare and Institutions Code Sections 11466.21(a) and 11466.5. Audited cost data will provide verifiable and reliable fiscal data to substantiate that California's group home and foster family agency (FFA) rates reflect reasonable costs as required by federal law and regulations.

Section 11-400f.(7)

Specific Purpose:

This section is being amended to include the annual financial audit definition within the fiscal audit definition.

Factual Basis:

This amendment is necessary for clarity and consistency with Welfare and Institutions Code Section 11466.2 for the recovery of sustained financial audit overpayments; to ensure that California meets the federal audit standard for the Foster Care (FC) program as required under Office of Management and Budget (OMB) Circular A-133; and to ensure that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification:

The definition of a fiscal audit is now being amended to repeal the financial audit definition from the fiscal audit definition. This amendment also repeals reference to the Department, as the distinction regarding who conducts the audit is unnecessary since it is already contained in Section 11-405. These amendments are necessary to clarify that a fiscal audit may still be conducted as necessary to investigate referrals made to the

Department in response to financial audit findings, or to validate cost data and other financial information.

Post-Hearing Modification

Section 11-400f.(13) (New)

Specific Purpose:

This section is being adopted to provide a definition for the term "fraud" and examples of fraud in relation to reporting financial information and misappropriation of assets.

Factual Basis:

The Department has a responsibility for safeguarding public funds. This amendment is necessary to highlight the types of illegal actions taken under false pretenses or illegally which result in the illegal expenditure of funds. The identification of fraud in a fiscal or financial audit of a non-profit corporation may result in Department actions to recover fraudulently expended funds. This definition is based on commonly accepted legal elements that comprise fraud and the American Institute of Certified Public Accountants' (AICPA) description and characteristics of fraud.

Post-Hearing Modification

Sections 11-400f.(14) and (15) (Renumbered)

Specific Purpose/Factual Basis:

These sections are renumbered from Sections 11-400f.(13) and (14) for consistency due to the addition of new Section 11-400f.(13).

Section 11-400m.(4)

Specific Purpose:

This section is being adopted to provide a definition for the term "Management Decision" which is a process for evaluating financial audit reports as specified in OMB Circular A-133, Subsection .405.

Factual Basis:

This section is necessary to ensure that California meets the federal audit standard for the FC program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This section is being amended to expand the Management Decision process to include the Department's evaluation of a provider's cost data and other financial information. This will help ensure that providers receive appropriate due process for non-OMB Circular A-133 related reviews.

Post-Hearing Modification

Section 11-400m.(5)

Specific Purpose:

This section is being adopted to provide a definition for the term "misuse" which addresses unauthorized acquisition, use or disposition of funds or assets for personal benefit. It also includes the use of AFDC-FC funds in a manner consistent with Section 11-404.

Factual Basis:

The Department has a responsibility for safeguarding public funds. This amendment is necessary to identify the types of situations or actions which constitute misuse in a fiscal or financial audit. As with fraud, the identification of misuse by a non-profit corporation may result in Department actions to recover misused funds. The definition is derived from *Government Auditing Standards*, Sections 4.25 and 4.26.

Post-Hearing Modification

Sections 11-400r.(1) through r.(1)(C)

Specific Purpose:

These sections are being repealed to eliminate the definition of "Rate Application."

Factual Basis:

This repeal is necessary for consistency and clarity to avoid redundancy. Group home and foster family agency rate application requests are currently defined in Sections 11-402 and 11-403.

Post-Hearing Modification

Section 11-400r.(2) (Renumbered)

Specific Purpose/Factual Basis:

This section is renumbered to Section 11-400r.(1) for clarity and consistency due to the repeal of the previous Section 11-400r.(1).

Section 11-400r.(3)

Specific Purpose:

This section is being amended for clarity and consistency with Welfare and Institutions Code Sections 11466.22 and 11466.31.

Factual Basis:

The amendment to this section is necessary for the efficient collection and processing of sustained overpayments from group home providers, which includes overpayments identified in the fiscal audit. As prescribed in Welfare and Institutions Code Section 11466.22(e), collection of sustained overpayments shall include procedures using several methodologies, one of which is a decrease in the AFDC-FC payment received by a group home provider without a Rate Classification Level (RCL) reduction. In addition, Welfare and Institutions Code Section 11466.31 provides for implementation of involuntary offset collection procedures to collect sustained overpayments. Department regulations currently provide for an RCL reduction, which is in conflict with the Welfare and Institution Code. This amendment corrects the conflict between the Department regulations and Welfare and Institutions Code. This section also applies to foster family agencies by reference cited in Section 11-403(j).

Final Modification:

This section is being renumbered to Section 11-400r.(2) because of the repeal of Section 11-400r.(1).

Section 11-400r.(4)

Specific Purpose:

This section is being adopted for clarity of Department regulations; consistency with Welfare and Institutions Code Section 11466.2; and provides an accurate definition for "RCL Reduction."

Factual Basis:

This section is necessary to describe an RCL reduction including identifying the circumstances under which a reduction may occur. This section is also necessary to differentiate an RCL reduction from an RCL rate payment offset.

Final Modification:

This section is being renumbered to Section 11-400r.(3) because of the repeal of Section 11-400r.(1).

Sections 11-400r.(5) through (8)

Specific Purpose/Factual Basis:

These sections are renumbered for clarity and consistency.

Final Modification:

These sections were previously renumbered because of new Section 11-400r.(4), which has now been renumbered to Section 11-400r.(3). As such, the previous renumbering is now not necessary and should revert to the original numbering as Sections 11-400r.(4) through 11-400r.(7).

Post-Hearing Modification

Section 11-402.222(a)

Specific Purpose:

This section is being amended to allow a social worker that meets the definition in Section 11-400s.(5) a base factor of 1.0 for each eligible hour.

Factual Basis:

This amendment is necessary to be consistent between the current definition of social worker [Section 11-400s.(5)]. The current social worker definition provides a variety of degree specifications that allow an individual to perform social work activities in group homes. However, the social worker weightings only provide weightings for a limited number of those degree specifications identified in the definition. Therefore, this amendment will allow those individuals with degree specifications that were not identified in this section to receive a base factor of one, and provides a clear and consistent relationship between the definition and those eligible to receive weightings.

Final Modification

The Department has stricken this section from the regulation package given that this change is unrelated to the implementation of OMB Circular A-133.

Post Hearing Modification

Sections 11-402.31 and .33

Specific Purpose:

These sections are being amended to cite the appropriate regulation sections that set forth the requirements for a complete rate application.

Factual Basis:

This amendment is necessary to maintain the accuracy of the regulations and to provide correct information to the persons who are subject to the ratesetting regulations.

Post-Hearing Modification

Section 11-402.351

Specific Purpose:

This section is amended for consistency and clarity purposes only.

Factual Basis:

The revision dates for all ratesetting forms have been removed from the text of the regulations and listed in a separate section. Setting out the forms/revision dates in a separate section allows ease in amending regulations when forms are adopted, repealed or revised, helping users of the regulations to know the most current form that must be used.

Post-Hearing Modification

Section 11-402.352

Specific Purpose:

This section is being amended to repeal the revision date of the SR 2 and to add the Group Home Program Days of Care Schedule (SR 5) to the list of documents required for a complete rate application.

Factual Basis:

This amendment is necessary to ensure that the Group Home Program Days of Care Schedule is included with the documents submitted for a complete rate application, formerly identified in Section 11-400r.(1), but which is now repealed.

Post-Hearing Modification

Sections 11-402.354 and .354(a)

Specific Purpose:

Section 11-402.354 is amended for clarity, and Section 11-402.354(a) is being amended to clarify the rate application process. This amendment will require the non-profit organization to provide a copy of either the Internal Revenue Service or the California Franchise Tax Board's (CFTB) letter designating their organization with a tax exempt status. The Department recognizes both the CFTB and the Internal Revenue Service (IRS) as governmental entities that may confer such status.

Factual Basis:

This amendment is necessary to clarify that the submission of the organization's tax exempt status letter may be granted by CFTB or IRS and the Articles of Incorporation substantiates their status as a non-profit organization that operates a group home program.

Post-Hearing Modification

Section 11-402.354(b)

Specific Purpose:

This section is being amended to clarify the rate application process. This amendment will require that the Articles of Incorporation as filed with the Secretary of State be submitted by the provider as evidence of their non-profit status in addition to, rather than in lieu of, evidence of their tax exempt status from CFTB or IRS.

Factual Basis:

This amendment is necessary to clarify that the submission of the organization's tax exempt status letter from CFTB or IRS and the articles of incorporation substantiates their tax exempt status as a non-profit organization that operates a group home program.

Post-Hearing Modification

Sections 11-402.354(b)(1) through 11-402.354(b)(1)(C)

Specific Purpose/Factual Basis:

This sections are being renumbered for clarity and consistency purposes.

Post-Hearing Modification

Sections 11-402.36 through .364(b)

Specific Purpose:

These sections are being repealed and moved to other sections to appropriately associate the requirements for submission of cost data reports with the requirement for financial audits. Combining the submission of the cost data reports with a financial audit will allow the cost data to be audited by a certified public accountant (CPA) and subsequently submitted to the Department for review. This repeal eliminates the requirement for submission of cost data as part of the of the rate application package, whereby some administrative relief is provided to the applicant.

Factual Basis:

The federal government requires that state governmental entities in receipt of federal funds provide safeguards for the expenditure of such funds. The Department will be utilizing the audited cost reports and financial audit report when a financial audit is conducted for a non-profit organization that operates a group home program. Therefore, it is no longer necessary to include the cost data reports for the purposes of establishing a rate.

Post-Hearing Modification

Sections 11-402.371(b) through (b)(4) and 11-402.372(c) through (c)(2)

Specific Purpose:

These sections are being repealed for clarity and consistency with the rate application process for a non-profit corporation that operates a group home program. The submission of a financial audit report will no longer be a requirement for the rate application process. As such, good cause procedures addressing the inadequacy of financial records are moot and no longer necessary under this section. However, good cause provisions for a non-profit corporation unable to submit a timely audit report are provided in Section 11-405.217.

Factual Basis:

The Department will not require a financial audit report to be submitted with a rate application package and consequently, it is no longer necessary to include good cause procedures for submission of an untimely financial audit report in this section.

Post-Hearing Modification

Section 11-402.393

Specific Purpose:

This section is being amended to add failure to submit a financial audit report as a reason for rate termination.

Factual Basis:

This amendment is necessary for consistency and to make specific the fact that failure to submit a financial audit report is a reason for rate termination as required by Section 11-405.2.

Post-Hearing Modification

Section 11-402.411

Specific Purpose:

This section is being amended to revise a reference citation due to the repeal of Section 11-402.36, and to require that projected data be reported on the Group Home Program Cost Report (SR 3) as a component of an initial rate application for a new program.

Factual Basis:

This amendment is necessary because the requirement to submit the annual financial audit report has been separated from the annual rate application because OMB A-133 establishes different submission criteria and timelines. However, new programs will still be required to submit projected cost data via the Group Home Program Cost Report (SR 3)in order for the department to establish a rate for a new program.

Post-Hearing Modification

Section 11-402.411(b)

Specific Purpose:

This section is being amended to clarify that providers who are discontinuing a group home program(s) in favor of a new program shall only submit the Group Home Program Days of Care Schedule (SR 5). Reference to the SR 3 and SR 4 has been repealed.

Factual Basis:

The Department has amended Section 11-402.411 to include the submission of the Group Home Program Days of Care Schedule (SR 5). Consequently, for a program that is being discontinued, the requirement for the SR 3 and SR 4 as well as language referencing cost data under this section is no longer necessary and has been repealed.

Post-Hearing Modification

Sections 11-402.411(e) and (e)(1)

Specific Purpose:

These sections are being repealed for clarity and consistency with the rate application process for a non-profit corporation that operates a group home program. The submission of a financial audit report will no longer be a requirement for the rate application process. As such, exemptions for submitting a financial audit report with the rate application package are moot and no longer necessary under this section.

Factual Basis:

The Department will no longer require financial audit reports to be submitted with a rate application package and therefore, exemptions are unnecessary. The provision for a new provider that has been incorporated fewer than 12 months to be exempt from submitting an audit has been moved to Section 11-405.215(a).

Post-Hearing Modification

Section 11-402.411(f) (Renumbered)

Specific Purpose/Factual Basis:

Existing Section 11-402.411(f) is renumbered to Section 11-402.411(e) because of the repeal of old Section 11-402.411(e).

Post-Hearing Modification

Section 11-402.422

Specific Purpose/Factual Basis:

This section amends a reference citation due to the repeal of Section 11-402.36.

Post-Hearing Modification

Section 11-402.422(b)

Specific Purpose:

This section is amended to repeal reference to "cost information forms," the previous requirement for submission of the SR 4, and form revision dates. This section is also amended to now provide for the submission of the Group Home Program Cost Report (SR 3) and Group Home Program Days of Care Schedule (SR 5).

Factual Basis:

The amendment to this section clarifies the reference to the required forms by identifying them by their title in addition to the form number. The SR 4 was repealed as it is not necessary for the establishment of a rate for a new provider. This section is necessary to inform the provider that projected data is to be submitted with a new provider rate application.

Post-Hearing Modification

Section 11-402.422(e)

Specific Purpose:

This section is being repealed because the requirement to submit an annual financial audit report is being separated from the annual rate application. The exemption for new providers was a one-time only provision for fiscal year 2000-01.

Factual Basis:

This repeal is necessary for clarity and consistency. The requirement for submission of an annual financial audit report with an annual rate application and the one-time only exemption for new providers have been repealed.

Section 11-402.422(f) (Renumbered)

Specific Purpose/Factual Basis:

This section is renumbered to Section 11-402.422(e) from Section 11-402.422(f) because of the repeal of the previous Section 11-402.422(e).

Post-Hearing Modification

Section 11-402.426

Specific Purpose/Factual Basis:

This section amends a reference citation due to the repeal of Section 11-402.36.

Post-Hearing Modification

Section 11-402.432(d)

Specific Purpose:

This section is being amended to clarify that providers who are discontinuing one group home program in favor of another or otherwise discontinuing a program shall only submit the Group Home Program Days of Care Schedule (SR 5). References to the SR 3 and SR 4 have been repealed.

Factual Basis:

This amendment is necessary for clarity and consistency.

Post-Hearing Modification

Sections 11-402.432(f) and (f)(1)

Specific Purpose:

These sections are being repealed because the requirement to submit an annual financial audit report is being separated from the annual rate application and the exemption for new providers was a one-time only provision for fiscal year 2000-01.

Factual Basis:

This repeal is necessary for clarity and consistency. The requirement for submission of an annual financial audit report with an annual rate application and the one-time only exemption for new providers have been repealed.

Post-Hearing Modification

Section 11-402.451

Specific Purpose:

This section is amended to provide the appropriate reference to Sections 11-405.217 through .219 for financial audit report program reinstatement requirements and repeals the reference to application requirements.

Factual Basis:

This amendment is necessary for clarity and consistency.

Post-Hearing Modification

Sections 11-402.62 and .629

Specific Purpose:

These sections are being adopted to clarify that AFDC-FC funds that are spent on items not permissible as specified in Section 11-404 shall be considered an overpayment.

Factual Basis:

These sections are necessary to ensure that recoupment of such funds is in accordance with existing overpayment procedures.

Section 11-402.636

Specific Purpose:

This section is being adopted to clarify that the determination of unallowable costs through a management decision for fiscal audits, when a group home provider or foster family agency has expended AFDC-FC funds on an unallowable cost, is an overpayment. This section applies to foster family agencies by reference as specified in MPP Section 11-403(j).

Factual Basis:

This section is necessary to ensure that California meets the federal audit standard for the FC program as required under OMB Circular A-133 for purposes of overpayment recovery and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This section is amended to clarify that if an overpayment is identified through a program audit and the Department has determined misuse or fraud during the same period, only the greater of the overpayments will be recovered. This amendment is necessary to ensure that a group home provider is not required to repay both an overpayment arising from a program audit and an overpayment arising from a financial audit as a result of misuse or fraud over the same time period.

Section 11-402.636(a)

Specific Purpose:

This section is being adopted to allow the Department to recover the unallowable costs resulting from a fiscal audit, unless the group home provider has also incurred a program audit overpayment during the same time period. This section applies to foster family agencies by reference as specified in MPP Section 11-403(j). This section also prevents duplication of overpayment recovery. If this situation occurs, the Department shall recover the greater of the amounts of either the fiscal audit unallowable costs or the program audit overpayment.

Factual Basis:

This section is necessary to ensure that a group home provider is not required to repay both an overpayment arising from a program audit and an overpayment arising from a financial audit where those overpayments were incurred over the same time period. This section is also necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This section was previously to be adopted as Section 11-402.636(a), but is now repealed for clarity and consistency and as a result of the amendment to Section 11-402.636.

Section 11-402.664(d)

Specific Purpose:

This section is being amended for clarity and consistency with Welfare and Institutions Code Sections 11466.22 and 11466.31.

Factual Basis:

This amendment is necessary to ensure efficient collection and processing of sustained overpayments, including overpayments arising from a financial audit. As prescribed in Welfare and Institutions Code Section 11466.22(e), collection of sustained overpayments shall include procedures using several methodologies, one of which is a rate decrease without an RCL reduction. This section also applies to foster family agencies by reference as specified in Section 11-403(j). In addition, Welfare and Institutions Code Section 11466.31 provides for implementation of involuntary offset collection procedures to collect sustained overpayments. Department regulations currently provide for an RCL reduction, which is in conflict with the Welfare and Institutions Code. This amendment corrects the conflict in the regulations.

Section 11-402.664(e)

Specific Purpose:

This section is being amended for clarity and consistency with Welfare and Institutions Codes Section 11466.22 and 11466.31.

Factual Basis:

This amendment is necessary for consistency in the implementation of involuntary offset collection procedures to collect sustained overpayments. Department regulations currently provide for an RCL reduction, which is in conflict with the Welfare and Institutions Code. This amendment corrects the conflict in the regulations whereby the Department will now issue a rate letter indicating the amount of the offset instead of RCL reduction.

Section 11-402.665(a)

Specific Purpose:

This section is being amended for clarity and consistency with Welfare and Institutions Sections 11466.22 and .31.

Factual Basis:

This amendment is necessary for the efficient collection and processing of sustained overpayments, including overpayments arising from a financial audit. As prescribed in Welfare and Institutions Code Section 11466.22(e), collection of sustained overpayments shall include procedures using several methodologies, one of which is a rate decrease without an RCL reduction. This section also applies to foster family agencies by reference as specified in Section 11-403(j). In addition, Welfare and Institutions Code Section 11466.31 provides for implementation of involuntary offset collection procedures to collect sustained overpayments. Department regulations currently provide for an RCL

reduction, which is in conflict with the Welfare and Institutions Code. This amendment corrects the conflict in the regulations.

Post-Hearing Modification

Section 11-402.81

Specific Purpose/Factual Basis:

This section is being amended to repeal reference to a calendar year reporting period and add reference to Section 11-405.214, which specifies a reporting period consistent with the provider's fiscal year. This section is also amended to repeal reference to a form which is no longer used for fiscal reporting.

Post-Hearing Modification

Section 11-402.811

Specific Purpose/Factual Basis:

This amendment is necessary to change a reference from a calendar year to a provider's fiscal year in addressing the reporting period when a provider has established a new program and has less than 12 months of data.

Post-Hearing Modification

Section 11-402.812

Specific Purpose/Factual Basis:

This section has been repealed because it is obsolete.

Section 11-402.82

Specific Purpose:

This section is being amended to provide clarity of allowable costs for AFDC-FC reimbursement and adds additional citations to aid in the determination of reimbursable costs for group home programs.

Factual Basis:

This amendment is necessary to ensure that all costs are actual allowable and reasonable; that California meets the federal audit standard for the foster care program as required under OMB Circular A-133; and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

These amendments are no longer necessary because of the federal DHHS' determination that the OMB Circular A-122 cost principles are not applicable to California's capitated rate structure.

Post-Hearing Modification

Section 11-402.828

Specific Purpose/Factual Basis:

This section is amended to add reference to various standards for determining what is reasonable in reporting AFDC-FC costs including the actions a prudent person would take in similar circumstances.

Post-Hearing Modification

Sections 11-402.828(c)

Specific Purpose:

This section is amended to provide parity for a non-profit corporation's executive compensation for the operation of a group home program. Existing regulations provided reasonable standards for executive salaries that were based on the Fiscal Year 1987-88 Los Angeles Area United Way guidelines for such salaries. This amendment is made to replace outdated standards contained currently in regulations.

Factual Basis:

This amendment is necessary as a result of Department of Treasury regulations issued in January 2001 interpreting the benefit limitation provisions of Section 4958 of the Internal Revenue Code for tax-exempt organization officials. Benefits from the organization include compensation, fringe benefits, or contracted payments. The Department finds that the standards set forth in the Department of Treasury Internal Revenue Code standards for tax-exempt organization's executive compensation provides a rational and fair measurement for purposes of determining the appropriateness of executive salary for non-profit corporations operating group homes and foster family agencies. The principles underlying federal tax-exempt status, and the conditions necessary to obtain federal tax-exempt status, are reasonably related to those conditions necessary to obtain and maintain non-profit status under California law.

Post-Hearing Modification

Sections 11-402.828(c)(1) through (c)(3) (Handbook)

Specific Purpose/Factual Basis:

These sections are obsolete "Handbook" references and are repealed for clarity and consistency with Section 11-402.828(c).

Post-Hearing Modification

Section 11-402.841 through .841(b)

Specific Purpose/Factual Basis:

These sections are being repealed because the references to the requirement for a cost basis of accounting conflict with Section 11-402.842, which pertains to an accrual basis of accounting. Section 11-402.841 will be reserved for future use.

Post-Hearing Modification

Section 11-402.846

Specific Purpose/Factual Basis:

This section is amended to repeal the term "Process" from the section title only and is necessary to clarify the section content.

Post-Hearing Modification

Sections 11-402.846(a) and (a)(1)

Specific Purpose:

This section is amended to specify that "AFDC-FC overhead" costs be allocated to each AFDC-FC program, and make reference to Welfare and Institutions Code Section 11460(b)(1), and replace "shall" to "may" for clarity.

Factual Basis:

This amendment is necessary for clarity and consistency and to reference Welfare and Institutions Code Section 11460(b)(1) to clarify what is meant by the term "overhead."

Post-Hearing Modification

Sections 11-402.846(a)(1)(A) through (C)

Specific Purpose/Factual Basis:

Sections 11-402.846(a)(1)(A) through (B) are amended only to add semi-colons at the end of the sentences to specify a string of alternative allocation bases. Section 11-402.846(a)(1)(C) is amended to add a semi-colon and the word "or" to note that a new section is to follow.

Post-Hearing Modification

Section 11-402.846(a)(1)(D)

Specific Purpose:

This section is adopted to include AFDC-FC revenue percentage as an alternative allocation basis.

Factual Basis:

Adoption of this section is necessary to provide an additional allocation basis from which non-profit corporations may choose to allocate AFDC-FC costs to each AFDC-FC program, if applicable.

Post-Hearing Modification

Section 11-402.846(a)(2)

Specific Purpose/Factual Basis:

This section is adopted to specify that the non-profit corporation's chosen methodology for allocation of AFDC-FC costs to each AFDC-FC program shall be documented in order to be subject to audit.

Post-Hearing Modification

Sections 11-402.85 and .851

Specific Purpose:

These sections have been repealed and reserved for future use.

Factual Basis:

These sections are repealed because cost data will not be submitted with the rate application package. Therefore, good cause or penalty procedures for late reporting or nonreporting of cost data are not necessary under this section.

Section 11-403(c)(1)

Specific Purpose:

This section is being amended to provide clarity of actual allowable costs for AFDC-FC reimbursement and adds additional citations to aid in the determination of reimbursable costs for foster family agencies.

Factual Basis:

This amendment is necessary to ensure that all costs are actual allowable and reasonable; that California meets the federal audit standard for the FC program as required under OMB Circular A-133; and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

These amendments are necessary to repeal reference to Section 11-405 as that reference is unnecessary and to clarify that this section addresses reporting of costs, not eligibility for reimbursement.

Post-Hearing Modification

Section 11-403(c)(1)(A)4.

Specific Purpose/Factual Basis:

This section is being adopted to provide reference to executive compensation standards and criteria contained in Internal Revenue Code Section 4958 applicable to foster family agencies. This reference to executive compensation is the same as that for group home programs as specified in Section 11-402.828(c).

Post-Hearing Modification

Section 11-403(f)(1)(B)

Specific Purpose:

This section is being amended to provide consistency in the rate request process for a non-profit organization that operates a foster family agency. Specifically, the submission

of a financial audit report is no longer required for the rate request process. The foster family agency rate request process is consistent with the group home process. Additionally, since the financial audit report does not need to be submitted to establish a rate for a foster family agency, the exceptions addressing inadequate financial records and good cause for late or incomplete financial records are moot and therefore, have been repealed.

Factual Basis:

This amendment is necessary because the requirement to submit an annual financial audit report has been separated from the annual rate request as a result of OMB Circular A-133 which establishes different submission criteria.

Post-Hearing Modification

Section 11-403(f)(1)(B)1.

Specific Purpose/Factual Basis:

Repeal of this section is necessary to separate the submission of the financial audit from the rate request. The repeal of this section is necessary to comply with the federal audit standard, OMB Circular A-133.

Post-Hearing Modification

Section 11-403(f)(1)(B)2. (Renumbered)

Specific Purpose/Factual Basis:

This section is renumbered only for clarity and consistency due to the repeal of Section 11-403(f)(1)(B)1.

Post-Hearing Modification

Sections 11-403(f)(1)(B)3. through 4.(ii)

Specific Purpose/Factual Basis:

Repeal of these sections is necessary to separate submission of the financial audit from the rate request. The repeal of these sections is necessary to comply with the federal audit standard, OMB Circular A-133.

Post-Hearing Modification

Section 11-403(f)(1)(D)

Specific Purpose/Factual Basis:

This section is being amended to provide clarity on the complete rate request submission process. This amendment is necessary as a technical clean-up.

Section 11-403(f)(1)(D)1.

Specific Purpose:

This section is amended to state that a foster family agency that submits a complete rate request after July 1 shall be subject to rate reestablishment requirements in Section 11-403(f)(3).

Factual Basis:

This amendment is necessary because current regulations do not permit the reestablishment of a rate for a foster family agency that submits a complete rate request after July 1. Under the current regulatory scheme, a foster family agency that does not submit a complete rate request before July 1 is subject to rate expiration and cannot reestablish a rate until the next annual ratesetting period. Providing rate reestablishment to a foster family agency provides an administrative process similar to that utilized in the ratesetting process to obtain a group home rate.

Final Modification

This section is being repealed as it is unnecessarily duplicative.

Section 11-403(f)(1)(D)2.

Specific Purpose:

This section is amended to require that a foster family agency that does not submit a complete rate request by July 1 that the agency will be denied a rate, and payment of AFDC-FC funds will cease effective September 1 until a complete rate request has been submitted.

Factual Basis:

This amendment is necessary to make more specific the process by which a foster family agency can reestablish a rate. Amending this subsection requires that the foster family agency meet all rate request requirements in order to have a rate reestablished. Requiring

a foster family agency to meet those requirements makes the ratesetting scheme consistent with the current regulatory ratesetting scheme to reinstate a group home rate.

Final Modification

This section is being renumbered and amended to require that a foster family agency that does not submit a complete rate request by July 1 will be denied a rate, and payment of AFDC-FC funds will cease effective September 1 except as provided in Section 11-403(f)(3). This amendment is necessary to clarify that a rate request must be complete in addition to meeting the July 1 due date and to clarify the exception of the rate reestablishment process.

Section 11-403(f)(2)(B)3.

Specific Purpose:

This section is being amended to provide clarity on the effective date of an annual rate for a late complete rate request.

Factual Basis:

This amendment is necessary to clarify the effective date of a rate that is late within the specified time period or is being reestablished.

Final Modification

This section is being amended for clarity and to make minor grammatical changes.

Section 11-403(f)(3)

Specific Purpose:

This section is being adopted to specify the requirements for reestablishing a rate after the untimely submission of a complete rate request.

Factual Basis:

This adoption is necessary to establish a process for reestablishing a rate and imposing a penalty for a foster family agency program that did not submit a complete rate request timely. There is no current regulatory process for the Department to reestablish the rate for a foster family agency that fails to timely comply with the annual complete rate request requirements, but complies with the requirements at a later time. Under current rules, the Department is required to discontinue the rate for the foster family agency that fails to submit a complete rate request, and to not establish a rate until the next annual rate application cycle occurs. The Department believes the current process poses an unfair punitive action on such providers. The penalty created by this regulatory

amendment would directly link the rate request application information with the setting of the rate and can be fairly and equitably applied to all providers with late complete rate requests. The process was selected because it is consistent with the reinstatement process afforded group homes in accordance with existing regulations.

Section 11-403(f)(3)(A)

Specific Purpose:

This section is adopted to provide a definition of the rate reestablishment process.

Factual Basis:

Adoption of this section is necessary because there is no current regulatory process for the Department to reestablish the rate for a foster family agency that fails to timely comply with the annual complete rate request requirements, but complies with the requirements at a later time.

Final Modification:

These amendments are necessary to make grammatical and cross reference changes. They also clarify that the rate request process is available only through the remainder of the fiscal year, and to eliminate unnecessary language and renumbering as a result. The amendments also clarify that a program rate will only be reestablished when all applicable rate request requirements have been met.

Section 11-403(f)(3)(A)1.

Specific Purpose:

This section is adopted to specify the effective date of a complete rate request submitted after July 1.

Factual Basis:

Adoption of this section is necessary because there is no current regulatory process for the Department to reestablish the rate for a foster family agency that fails to timely comply with the annual complete rate request requirements, but complies with the requirements at a later time.

Final Modification

These amendments are necessary to make grammatical changes. They also change the effective date of a rate under the reestablishment process to no earlier than September 1 rather than October 1 to ensure that no loss of funding occurs to an FFA if the FFA submits a timely request for reestablishment of the rate.

Sections 11-403(f)(3)(A)2. through 2.(ii)

Specific Purpose:

These sections are adopted to specify how a foster family agency's rate will be determined when the agency is subject to rate reestablishment requirements.

Factual Basis:

Adoption of these sections is necessary because there is no current regulatory process for the Department to reestablish the rate for a foster family agency that fails to timely comply with the annual complete rate request requirements, but complies with the requirements at a later time.

Post-Hearing Modification

Section 11-403(f)(3)(A)3.

Specific Purpose:

This section is adopted to specify that a foster family agency whose rate was terminated because of an unacceptable financial audit report shall not have the rate reestablished until audit reporting requirements have been met.

Factual Basis:

Adoption of this section is necessary because there is no current regulatory process for the Department to reestablish the rate for a foster family agency that fails to timely comply with the financial audit requirements; and is terminated but complies with the requirements at a later time.

Post-Hearing Modification

Section 11-403(f)(3)(A)3.(i)

Specific Purpose:

This section is adopted to specify that once the foster family agency's financial audit reporting requirements have been met, the rate may be reestablished effective the date the Department provides written notice to the corporation.

Factual Basis:

Adoption of this section is necessary because there is no current regulatory process for the Department to reestablish the rate for a foster family agency that fails to timely and completely comply with the financial audit requirements and is terminated, but complies with the requirements at a later time.

Post-Hearing Modification

Sections 11-403(g)(1)(B) through (g)(1)(B)3.

Specific Purpose:

The proposed amendments in this section repeal duplicative and obsolete requirements created by adoption of amendments made in other sections herein.

Factual Basis:

Existing regulations provide two methods for establishing a rate for a foster family agency. Both methods use social worker costs as the determinative factor for the amount of the rate. One method is applicable to a new foster family agency requesting its first rate and the other method is applicable to an existing foster family agency continuing its rate on an annual basis. With adoption of new regulations proposed in this package which separates cost data collection from the rate request process, the need for the two methods is no longer necessary.

Post-Hearing Modification

Sections 11-403(g)(1)(C) through (g)(1)(C)3.

Specific Purpose:

These sections are amended to repeal reference to a "permanent" rate and remove the requirement that a complete rate request be based on actual costs for social work in specified cost periods. The section now provides that a complete rate request is to be submitted in accordance with Section 11-403(f)(1)(B).

Factual Basis:

These amendments are necessary since proposed amendments to the existing regulations repeal the requirement that cost information be submitted with a rate application. These amendments propose instead that the cost information be submitted as part of a financial audit, to comply with federal OMB A-133 requirements. Existing rate setting regulations require a new foster family agency provider to submit actual cost information on an annual basis to receive a permanent rate. Because the cost information will not be part of a rate request, the distinction between an initial rate and a permanent rate is unnecessary.

Sections 11-403(g)(1)(C)1. through 3. are repealed because it is no longer necessary to identify cost reporting periods for purposes of the rate application process or variable rate request due dates.

Post-Hearing Modification

Sections 11-403(g)(1)(D) through (D)1.

Specific Purpose/Factual Basis:

These sections are being repealed because the requirement to submit an annual financial audit report is being separated from the requirement to submit an annual rate request. Therefore, the exceptions are no longer necessary.

Post-Hearing Modification

Section 11-403(g)(2)(B)

Specific Purpose:

This section is amended for compatibility with other amendments made herein. This section is being amended to make the rate request process clearer and more consistent with existing foster family agency rate request requirements. The distinction of an initial rate is no longer required as all rates will be established according to the schedule of rates on an annual basis for all providers.

Factual Basis:

These amendments are necessary since proposed amendments to the existing regulations repeal the requirement that cost information be submitted with a rate request. It is instead proposed that the cost information be submitted as part of a financial audit. Existing rate setting regulations require a new program to submit projected cost information upon initial application for a rate, and then submit actual cost information subsequently on an annual basis for a permanent rate. Because the cost information will not be part of a rate application, the distinction of an initial rate is unnecessary.

Post-Hearing Modification

Sections 11-403(g)(2)(D) through (D)1.

Specific Purpose:

These sections are being repealed because the requirement to submit an annual financial audit report is being separated from the requirement to submit an annual rate request. Therefore, the exemptions are no longer necessary.

Factual Basis:

The repeal of these sections is necessary for clarity and consistency. The requirement for submission of an annual financial audit report with an annual rate request is no longer required. It also repeals the one-time only exception for new providers. The provision for a provider who has been incorporated for less than twelve months is moved to Section 11-405.215.

Section 11-403(j)(1)

Specific Purpose:

This section is being amended to correct a reference citation.

Factual Basis:

This amendment is necessary for accuracy in the regulations to eliminate reference to obsolete regulatory citations.

Final Modification

This amendment is necessary to clarify when an FFA overpayment exists and to clarify that AFDC-FC funds that are spent on items not permissible as specified in Section 11-404 shall be considered an overpayment. This clarification is necessary to ensure that recoupment of such improper expenditures is in accordance with existing overpayment collection procedures.

Post-Hearing Modification

Section 11-403(k) and (k)(1)

Specific Purpose/Factual Basis:

This section is being amended to correct the use of an ambiguous term and a reference citation.

Post-Hearing Modification

Sections 11-403(l) through (l)(1)(E)

Specific Purpose:

These sections are being adopted to establish good cause procedures for a foster family rate request that was not submitted timely. These sections are necessary to make clear that foster family agencies have the same rights for good cause afforded to group homes and is consistent with Section 11-400(g)(1) which defines good cause.

Factual Basis:

These amendments are necessary to define good cause procedures for a late foster family agency rate request. Currently, good cause regulations exist for group home providers but are absent for foster family agencies. These regulations will provide relief for a foster family agency that meets the definition of good cause when it is unable to submit a timely rate request.

Post-Hearing Modification

Section 11-403(l)(2)

Specific Purpose:

This section is adopted to provide a timeframe for the Department to approve or deny the foster family agency's request for a good cause extension and to provide a written determination to the provider.

Factual Basis:

Adoption of this section is necessary to provide good cause regulations for foster family agency rate requests. This amendment is consistent with existing good cause regulations for group home rate applications.

Post-Hearing Modification

Section 11-403(l)(2)(A)

Specific Purpose:

This section is adopted to allow a foster family agency with an approved good cause request 30 additional days to submit a complete rate request. This amendment also establishes an effective date for the rate when a complete rate request is submitted within the 30-day time frame.

Factual Basis:

Adoption of this section is necessary to provide good cause regulations for foster family agency rate requests. This amendment is consistent with existing good cause regulations for group home rate applications.

Post-Hearing Modification

Section 11-403(l)(2)(B)

Specific Purpose:

This section is adopted to establish the rate effective date for a foster family agency that does not submit a complete rate request within the 30-day good cause extension time frame.

Factual Basis:

Adoption of this section is necessary to provide good cause regulations for foster family agency rate requests. This amendment is consistent with existing good cause regulations for group home rate applications.

Post-Hearing Modification

Section 11-403(l)(2)(C)

Specific Purpose:

This section is adopted to require a foster family agency whose good cause request is denied to submit a complete rate request prior to the first of the next calendar month to avoid additional late penalties. This amendment also establishes an effective date for the rate when good cause is denied.

Factual Basis:

Adoption of this section is necessary to provide good cause regulations for foster family agency rate requests. This amendment is consistent with existing good cause regulations for group home rate applications.

Post-Hearing Modification

Section 11-404

Specific Purpose/Factual Basis:

This section is adopted to provide the necessary title, "Use of Federal and State Foster Care Funds."

Post-Hearing Modification

Section 11-404.1

Specific Purpose:

This section is adopted to specify that State and federal AFDC-FC program funds provided to non-profit corporations who operate a group home and/or foster family agency are to be used to meet the cost of providing care and supervision as indicated to eligible children, including the associated administrative costs.

Factual Basis:

Adoption of this section is necessary for clarity and consistency with the federal Department of Health and Human Services' determination of the use of AFDC-FC program funds and to ensure that Title IV-E federal financial participation is not jeopardized.

Post-Hearing Modification

Sections 11-404.2 through .24

Specific Purpose:

These sections are adopted to identify the purposes for which any unexpended AFDC-FC program funds may be used by a non-profit corporation operating a group home and/or foster family agency, regardless of the fiscal year in which the funds were received.

Factual Basis:

Adoption of these sections are necessary to avoid inappropriate use of State foster care funds and to comply with Welfare and Institutions Code Section 11460 which describes the activities providers are required to perform in return for the receipt of foster care payments. This section is also necessary to clarify the use of unexpended AFDC-FC program funds by non-profit corporations operating a group home and/or foster family agency. This section will enable the Department to ensure that unexpended AFDC-FC program funds are directed towards programs and/or activities that serve or benefit California foster care children for which the funds were initially intended.

Post-Hearing Modification

Section 11-404.3

Specific Purpose:

This section is adopted to provide the definition of the term "foster care children" for the purposes of administering Section 11-404.

Factual Basis:

Adoption of this section is necessary for clarity and consistency of the use of State and federal AFDC-FC program funds for children or youth who are placed in out-of-home care by a California child welfare services or probation placement agency, which includes foster care children, foster youth, and children placed out of state pursuant to the Interstate Compact on the Placement of Children.

Section 11-405.11

Specific Purpose:

This section is being amended to include fiscal audits of foster family agencies in addition to group homes.

Factual Basis:

This amendment is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

For purposes of fiscal audits, certified public accountants and others specified in the original amendment are already considered the Department's agents and as such this amendment is not necessary.

Section 11-405.112

Specific Purpose:

This section is being amended to require that foster family agencies, in addition to group home programs, must maintain documentation, as appropriate, to support AFDC-FC program expenditures for a period of not less than five years.

Factual Basis:

This amendment is necessary to ensure that foster family agencies are subject to the records retention requirements that are consistent with the federal audit standard for the foster care program as required under OMB Circular A-133. This is necessary to ensure that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

Since the documentation requirements for foster family homes and group homes are different, this amendment is necessary to clarify the distinction.

Section 11-405.13

Specific Purpose:

This section is being amended to include other allowable cost categories identified in OMB Circular A-122, Cost Principles for Non-Profit Organizations, Attachment B.

Factual Basis:

This amendment is necessary to ensure that group homes and foster family agencies are referred to the federally-required cost categories. This amendment is also necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This section is being amended for clarity and consistency with the federal DHHS' determination that the A-122 Cost Principles are not applicable within California's capitated rate structure and now identifies the appropriate cost reports to be used by non-profit organizations to report costs expended for the foster care program.

Section 11-405.136

Specific Purpose:

This section is being amended to include other group home and foster family agency payroll and fringe benefit costs not otherwise identified as allowable costs for reimbursement.

Factual Basis:

This amendment is necessary to specify that payroll and fringe benefit cost records shall be maintained. This amendment is also necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Post-Hearing Modification

Section 11-405.2

Specific Purpose:

This section is adopted to comply with Welfare and Institutions Code Section 11466.21, which requires providers to submit a financial audit report as a condition to receive an AFDC-FC rate.

Factual Basis:

Adoption of this section is necessary to ensure compliance with Welfare and Institutions Code Section 11466.21 since Section 11-402.364 regarding submittal of a financial audit report as a required component of the group home rate application process is being repealed, and Section 11-403(f)(1)(B) is being amended to omit reference to the financial audit report as a required component of the foster family agency rate request process.

Section 11-405.21

Specific Purpose:

This section is being amended to exclude the reference that acceptance of financial audits is tied only to ratesetting purposes.

Factual Basis:

This amendment is necessary to provide clarity and consistency for group home and foster family agency corporations that financial audits are not accepted for ratesetting purposes only. Financial audits may also be accepted in accordance with OMB Circular A-133 requirements, which do not speak to ratesetting purposes. This amendment is also necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Section 11-405.213

Specific Purpose:

This section is being amended to provide the specific title of the audit standards to be used by group home and foster family agency corporations for the performance of financial audits.

Factual Basis:

This amendment is necessary to provide clarity and consistency for group home and foster family agency corporations by identifying that financial audits are to be conducted according to the Government Auditing Standards issued by the Comptroller General of the United States (commonly known as the Generally Accepted Government Auditing Standards (GAGAS) audit).

Final Modification

The additional amendment now ensures the application of all financial accounting standards for entities organized and operated on a non-profit basis, in addition to GAGAS. This is consistent with accounting and auditing industry practices.

Section 11-405.213(a)

Specific Purpose:

This section is being amended to inform group home and foster family agency corporations that all audits shall be conducted according to Government Auditing Standards issued by the Comptroller General of the United States, often referred to as generally accepted government auditing standards (GAGAS) and financial accounting standards applicable to entities organized and operated on a nonprofit basis.

Factual Basis:

This amendment is necessary to ensure that group home and foster family agency corporations continue to conduct audits in accordance with the Government Auditing Standards issued by the Comptroller General of the United States (GAGAS).

Final Modification

This section is being amended to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized. This section is amended to repeal the statement that all audits shall be conducted according to GAGAS and applicable non-profit financial accounting standards. References to these standards were moved to Section 11-405.213. This section now provides guidance on determining when

an OMB Circular A-133 audit is required for group homes and foster family agency corporations and specifies the reporting requirements, including report due dates.

Post-Hearing Modification

Section 11-405.213(a)(1)

Specific Purpose:

This section is adopted to inform a group home or a foster family agency corporation that its program shall be deemed to have expended federal funds when it receives the funds.

Factual Basis:

This section is necessary to identify when federal funds are considered expended for purposes of determining whether an OMB Circular A-133 audit is required.

Post-Hearing Modification

Section 11-405.213(a)(2)

Specific Purpose:

This section is adopted to instruct group home and foster family agency corporations to submit to the Department a copy of the OMB Circular A-133 report and audited cost data.

Factual Basis:

This amendment enables the Department to assess the financial condition of the non-profit corporation and take corrective action measures as necessary.

Post-Hearing Modification

Section 11-405.213(a)(3)

Specific Purpose:

This section is adopted to specify that group home and foster family agency corporations that meet the federal funding threshold requiring an OMB Circular A-133 audit, but whose fiscal year began prior to the adoption of new federal audit requirement regulations, are required to submit a financial audit in accordance with Government Auditing Standards or OMB Circular A-133 standards.

Factual Basis:

Adoption of this section is necessary to provide instructions on which audit standards to follow for the group of providers who will meet the funding threshold for an OMB Circular A-133 audit, but whose fiscal year began prior to the effective date of regulations. These providers would have difficulty complying with the new regulations and may have already completed their audit or engaged a CPA to conduct their audit when regulations take effect.

Section 11-405.213(b)

Specific Purpose:

This section is being amended to provide the federal funding threshold which determines whether an OMB Circular A-133 audit is required for group home and foster family agency corporations.

Factual Basis:

This amendment is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This section is amended to specify the audit standards for a non-profit corporation that is exempt from an OMB Circular A-133 audit. This amendment is necessary to inform group home and foster family agency corporations who do not meet the federal funding threshold for an OMB Circular A-133 audit that the audit to be submitted must be conducted according to Government Auditing Standards. This amendment also specifies appropriate due dates for submission of the financial audit report. This section is now amended to repeal the reference to the funding threshold for determining when an OMB Circular A-133 audit is required since that reference has been moved to Section 11-405.213(a).

Section 11-405.213(b)(1)

Specific Purpose:

This section is being adopted to provide OMB Circular A-133 audit report due dates and submission requirements.

Factual Basis:

This section is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This section is being repealed since the references to report due dates for audits which require OMB Circular A-133 standards were moved to Section 11-405.213(a).

Section 11-405.213(b)(2)

Specific Purpose:

This section is being adopted to provide instruction to group home and foster family agencies on where report packages are to be submitted within the Department.

Factual Basis:

This section is necessary to inform providers that a copy of the financial audit is to be submitted to the Foster Care Audits Branch, and is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This section is being repealed since the references to report due dates for audits which require OMB Circular A-133 standards were moved to Section 11-405.213(a).

Section 11-405.213(b)(3)

Specific Purpose:

This section is being adopted to provide instruction to group home and foster family agencies to send one copy of the audit report with the annual rate application package.

Factual Basis:

This section is necessary to inform providers that a copy of the financial audit is to be submitted with the annual rate application. This procedure is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This section is being repealed since the references to report due dates for audits which require OMB Circular A-133 standards were moved to Section 11-405.213(a). This amendment is also necessary to repeal the requirement for providers to submit a copy of the audit report with the annual foster care rate application package since the audit report has been separated from the annual rate application process.

Post-Hearing Modification

Section 11-405.214

Specific Purpose:

This section is amended to specify that cost data previously reported as a component of the rate application, shall now be audited and reported as part of the financial audit.

Factual Basis:

This amendment is necessary to add specific cost data reporting requirements for the financial audit. The cost reports, Group Home Program Cost Report (SR 3), Group Home Program Payroll and Fringe Benefit Report (SR 4), and the Total Program Cost Display (FCR 12FFA), must be audited and submitted with their financial audit report.

Post-Hearing Modification

Section 11-405.214(a)

Specific Purpose:

This section is adopted to provide specific instructions on cost data to be submitted as part of the required financial audit report when the non-profit corporation's fiscal year began prior to the effective date of the regulations implementing the new audit requirements.

Factual Basis:

Adoption of this section is necessary to specify that a non-profit corporation operating a group home or foster family agency program whose fiscal year began prior to adoption of these regulations will not be required to submit audited cost data with the financial audit report since the completion of their audit may occur prior to the effective date of regulations. The corporation shall instead submit unaudited cost data.

Section 11-405.215

Specific Purpose:

This section is being adopted to provide the additional audit requirement and guidance for incorporating audit compliance testing for all GAGAS audits, as well as all OMB Circular A-133 audits, according to the OMB Circular A-133 Compliance Supplement.

Factual Basis:

This section is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This amendment has been repealed because specific reference to audit compliance testing is already specified in OMB Circular A-133. With the repeal of this amendment, the previous renumbering of this section for clarity and consistency is no longer necessary. The original Section 11-405.215 will be reinstated.

Post-Hearing Modification

Section 11-405.215(a)

Specific Purpose:

This amendment is necessary to remove language associated with the submission of a financial audit report to receive an annual foster care rate. In addition, this amendment is necessary to exempt certain providers who would have limited financial information arising from an incomplete fiscal period, from being required to submit a financial audit report.

Factual Basis:

Since the requirement for a financial audit report is being separated from the annual foster care rate application, this amendment is necessary to repeal language allowing providers to submit an audit report for the prior year if the report has not been submitted previously to obtain a foster care rate. Notwithstanding provisions of OMB Circular A-133 as noted in reference to Section 11-405.21, the amendment also specifies that providers, who have been incorporated fewer than twelve calendar months by the end of its first fiscal year in which it received AFDC-FC funds, would be exempt from the financial audit report requirement.

Section 11-405.216

Specific Purpose/Factual Basis:

This section is renumbered from Section 11-405.212 for clarity and consistency.

Final Modification

Originally, this section was renumbered from Section 11-405.216 to Section 11-405.217 for clarity and consistency. Since the previous Section 11-405.215 amendment has been repealed and replaced with its original language in the final modification, this section is renumbered back to Section 11-405.216 for numbering consistency. In addition, language was modified to make minor technical corrections.

Section 11-405.217

Specific Purpose:

This section is being amended to provide the specific title of the audit standards to be used by group home and foster family agency corporations for financial audits. Also incorporated is the new regulatory citation for the federal OMB Circular A-133 audit requirement. The section is also renumbered from Section 11-405.216 for clarity and consistency.

Factual Basis:

This section as amended, is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized. The section is also renumbered for clarity and consistency.

Final Modification

This section is renumbered back to Section 11-405.216 because of the repeal of the previous Section 11-405.215.

Post-Hearing Modification

Section 11-405.217 (New)

Specific Purpose/Factual Basis:

This section is adopted to specify that, for those situations when the provider has good cause for submitting an audit report after the due date the provider may submit a written request for such a determination. This amendment is also necessary as the audit

requirement is being separated from the rate application process where there was a provision for good cause on submitting an untimely audit report.

Post-Hearing Modification

Sections 11-405.217(a) through .217(a)(6)

Specific Purpose/Factual Basis:

These sections are necessary to provide a list of the specific information that must be included in the written request for a determination of good cause for late submission of a financial audit report.

Post-Hearing Modification

Sections 11-405.217(b) through (b)(2)

Specific Purpose/Factual Basis:

These sections are adopted to specify the time period when the Department must notify the provider in writing of the determination of a good cause decision. These amendments are also necessary to clarify the Department's responsibility for notifying the provider of the revised due date when good cause exists and of the consequences when good cause does not exist.

Sections 11-405.218 and .219

Specific Purpose:

These sections are being amended to correct reference citations and to renumber from Sections 11-405.217 and .218 for clarity and consistency.

Factual Basis:

These amendments are necessary for accuracy, clarity and consistency in the regulations.

Final Modification

These sections are being further amended to change the wording from "provider" to "non-profit corporation" for language consistency in the regulations and to correct citation errors.

Section 11-405.22

Specific Purpose:

This section is being adopted to provide a partial listing of group home and foster family agency corporation and Department responsibilities for ensuring that the requirements of the OMB Circular A-133 audit are met. Specific responsibilities are delineated under OMB Circular A-133.

Factual Basis:

These sections are necessary to implement a requirement that group home and foster family agencies meet the auditee responsibilities set forth in OMB Circular A-133. This section also ensures that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This amendment is being repealed. There is no need for a partial listing of group home and foster family agency non-profit corporation and Department responsibilities to be included in the regulations since a complete listing of each entity's responsibilities for ensuring that the requirements of the OMB Circular A-133 audit are met is contained in the circular itself. Also, this amendment is necessary to correct a technical error in the original amendment.

Section 11-405.221 (Handbook)

Specific Purpose:

This section is being added to provide group homes and foster family agencies with a partial listing of group home and foster family agency corporation responsibilities within OMB Circular A-133, Subpart C, Section .300.

Factual Basis:

This section is necessary to ensure that group homes and foster family agencies are aware of their responsibilities under OMB Circular A-133. This information is necessary to ensure that the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification to Section 11-405.22.

Section 11-405.221(a) (Handbook)

Specific Purpose:

This section is being added to specifically identify the group home/foster family agency responsibility for maintaining internal control over federal funds and refers corporations to OMB Circular A-133, Subpart C, Section .300, for specific requirements.

Factual Basis:

This section is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This section has been deleted and the content has been moved to Section 11-405.231(a).

Section 11-405.221(b) (Handbook)

Specific Purpose:

This section is being added to specifically identify the group home/foster family agency responsibility for preparing a schedule of expenditures of federal funds and refers corporations to OMB Circular A-133, Subpart C, Section .310, for specific requirements.

Factual Basis:

This section is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This section has been deleted and the provider's hearing rights are now contained in Section 11-405.232.

Section 11-405.221(c) (Handbook)

Specific Purpose:

This section is being added to specifically identify the group home/foster family agency responsibility for preparing a financial statement for the most recent fiscal year and refers corporations to OMB Circular A-133, Subpart C, Section .310, for specific requirements.

Factual Basis:

This section is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification to Section 11-405.22.

Section 11-405.221(d) (Handbook)

Specific Purpose:

This section is being added to specifically identify the group home/foster family agency responsibility for follow-up and corrective action on all audit findings and refers corporations to OMB Circular A-133, Subpart C, Section .315, for specific requirements.

Factual Basis:

This section is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification to Section 11-405.22.

Section 11-405.221(e) (Handbook)

Specific Purpose:

This section is being added to specifically identify the group home/foster family agency responsibility for compliance with audit data collection, report submission, and reporting package requirements, and refers corporations to OMB Circular A-133, Subpart C, Section .320, for specific requirements.

Factual Basis:

This section is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification to Section 11-405.22.

Section 11-405.222 (Handbook)

Specific Purpose:

This section is being added to provide group homes and foster family agencies with a partial listing of Department responsibilities within OMB Circular A-133, Subpart D, Section .400.

Factual Basis:

This section is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification to Section 11-405.22.

Section 11-405.222(a) (Handbook)

Specific Purpose:

This section is being added to specifically identify the Department's responsibility for issuing management decisions on audit findings and refers corporations to OMB Circular A-133, Subpart D, Section .405, for information.

Factual Basis:

This section is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This section has been deleted and the content has been moved to Section 11-405.231(a).

Section 11-405.222(b) (Handbook)

Specific Purpose:

This section is being added to specifically identify the Department's responsibility for the establishment of an appeal process for management decisions and refers corporations to OMB Circular A-133, Subpart D, Section .405, for information.

Factual Basis:

This section is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

This section has been deleted and the provider's hearing rights are now contained in Section 11-405.232.

Section 11-405.23

Specific Purpose/Factual Basis:

This section is being renumbered from Section 11-405.22 for clarity and consistency.

Final Modification

This section is renumbered back to Section 11-405.22 because of the repeal of the previous Section 11-405.22.

Post-Hearing Modification

Sections 11-405.23, .231(a), .231(b), and .231(c)

Specific Purpose:

These sections are necessary to establish administrative procedures for recoupment of costs identified in a fiscal or financial audit as disallowed costs, including misuse or fraud involving AFDC-FC funds. The procedures include the issuance of a management decision which will clearly state whether the audit finding is sustained, the reasons for the decision, and the expected corporation action to repay disallowed costs, make financial adjustments, or take other action. The Department's determination of disallowed costs and its decision on recoupment will be based on a review of the audit findings, any responses from the non-profit corporation's management to the findings, including any action taken to recover misused or fraudulently expended funds, and findings from any additional audits conducted by the Department or its designee.

Factual Basis:

In accordance with OMB Circular A-133, the Department or its designee, is the agency responsible for ensuring that identified improper expenditures are recouped as part of the auditee's responsibility to make appropriate corrective action. This amendment is necessary to authorize the Department to take appropriate recoupment action based on the management decision process.

Post-Hearing Modification

Section 11-405.232

Specific Purpose/Factual Basis:

This adoption is necessary to afford due process by establishing a process for appeals of the Department's decisions on audit findings where disallowed costs related to AFDC-FC funds is disclosed in a fiscal or financial audit. The due process established in this section is a common and well-established procedure relating to this regulated industry.

Post-Hearing Modification

Section 11-405.233

Specific Purpose:

This new section establishes repayment terms in accordance with Section 11-402.66.

Factual Basis:

This amendment provides a reasonable balance between the public's need to recover funds and the non-profit corporation's ability to make repayment while continuing operations.

Post-Hearing Modification

Sections 11-405.234 through .234(b)

Specific Purpose/Factual Basis:

These sections establish authority, criteria, and guidance for rate termination where a non-profit corporation has had findings of misuse or fraudulently expended AFDC-FC funds disclosed from a fiscal or financial audit. These sections also establish authority, criteria, and guidance for rate termination where a non-profit corporation has failed to substantially comply with corrective action as specified in the management decision letter. Authority for rate termination when corrective action is not taken relative to findings contained in the management decision letter is necessary to comply with OMB Circular A-133 which requires that the Department as a pass-through agency must ensure that the sub-recipient takes timely corrective action.

Section 11-405.24

Specific Purpose:

This section is being adopted to provide an appeal process for fiscal audit management decisions. The process involves a request for formal hearing and is available to all group home and foster family agency corporations who receive a Department management decision on audit findings resulting in disallowed costs.

Factual Basis:

This section is necessary to establish formal hearing procedures for appeals of management decisions on audit findings. It also ensures that California meets the federal audit standard for the foster care program as required under OMB Circular A-133, that Title IV-E federal financial participation in the program is not jeopardized, and that all providers receive due process.

Final Modification

This amendment and amendments to Sections 11-405.241 through 11-405.249 are repealed. The appeals process for management decision findings identifying questioned costs resulting from an OMB Circular A-133 audit are now addressed in the new Section 11-405.232. This section now clarifies a county's authority relative to OMB Circular A-133 audits. This section is necessary to clarify that a county may perform contract compliance audits to the extent that they do not duplicate an OMB Circular A-133 audit.

Section 11-405.241

Specific Purpose:

This section is being adopted to provide a 30-day timeframe for group home and foster family agency corporations to submit a request for formal hearing. If the request for formal hearing is not received within the specified time period, the Department's management decision shall be final.

Factual Basis:

This section is necessary to establish a process for appeals of the Department's management decisions on audit findings, and ensures a timely response by group home and foster family agency corporations on management decisions. The section is also necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification for Section 11-405.24.

Section 11-405.242

Specific Purpose:

This section is being adopted to require that group home and foster family agency corporations submit the request for formal hearing via personal delivery or certified mail to both the office of hearings specified in the audit report and the Department.

Factual Basis:

This section is necessary to establish a formal hearing process for appeals of the Department's management decisions on audit findings, and ensures the group home and foster family agency corporation that the request for hearing was received by the appropriate hearing entities by the regulatory timeframe. This section is also necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification for Section 11-405.24.

Section 11-405.243

Specific Purpose:

This section is being adopted to inform group home and foster family agency corporations that the Department will not accept any documents relevant to the management decision after the date the corporation has filed the request for hearing.

Factual Basis:

This section is necessary to establish a formal hearing process for appeals of the Department's management decisions on audit findings, and is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification for Section 11-405.24.

Section 11-405.244

Specific Purpose:

This section is being adopted to inform group home and foster family agency corporations that the formal hearing on the management decision will be conducted within 60 days of receipt of the request for hearing.

Factual Basis:

This section is necessary to establish a formal hearing process for appeals of the Department's management decisions on audit findings and ensures group home and foster family agency corporations that a hearing will be conducted promptly. It is also necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification for Section 11-405.24.

Section 11-405.245

Specific Purpose:

This section is being adopted to provide that the standard of proof shall be the preponderance of the evidence and the burden of proof shall be on the Department to support its management decision.

Factual Basis:

This section is necessary to establish a formal hearing process for appeals of the Department's management decisions on audit findings and is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133. It is also necessary to ensure that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification for Section 11-405.24.

Section 11-405.246

Specific Purpose:

This section is being adopted to identify what documentation should be contained in the administrative record.

Factual Basis:

This section is necessary to establish a formal hearing process for appeals of the Department's management decisions on audit findings, and ensures that an appropriate legal administrative record is maintained. This section is also necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification for Section 11-405.24.

Section 11-405.247

Specific Purpose:

This section is being adopted to provide and inform group home and foster family agency corporations of the regulations by which the formal hearing shall be conducted.

Factual Basis:

This section is necessary to establish a formal hearing process for appeals of the Department's management decisions on audit findings, and ensures that the hearing is conducted according to established procedures. The section is also necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification for Section 11-405.24.

Section 11-405.248

Specific Purpose:

This section is being adopted to provide and inform group home and foster family agency corporations of the specified timeframe for issuance of the proposed decision by the hearing officer.

Factual Basis:

This section is necessary to establish a formal hearing process for appeals of the Department's management decisions on audit findings and ensures a prompt decision within 45 days of the close of the hearing record. This section is also necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification for Section 11-405.24.

Section 11-405.249

Specific Purpose:

This section is being adopted to provide and inform group home and foster family agency corporations of the timeframe for adoption, rejection, or modification of the proposed decision by the Department Director.

Factual Basis:

This section is necessary to establish a formal hearing process for appeals of the Department's management decisions on audit findings and ensures that the proposed decision is adopted promptly within 45 days of the issuance of the decision. This section also allows additional time for the Department Director to reject or adopt a modified proposed decision within 100 days. If the Director takes no action on the proposed decision within the prescribed timeframes, the proposed decision shall take effect by operation of law. This section is also necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 and that Title IV-E federal financial participation in the program is not jeopardized.

Final Modification

See Final Modification for Section 11-405.24.

Post-Hearing Modification

Section 11-406

Specific Purpose:

This section is adopted to alphabetically identify specific forms, definitions of forms, and revision dates required by the Department for use by group home and foster family agency non-profit corporations in submission of rate, cost and audit information to the Department as required by regulation.

Factual Basis:

Adoption of this section is necessary due to a new State Office of Administrative Law requirement that each State entity having MPP regulations oversight will separately identify a new section detailing the required forms, titles, definitions, and revision dates required by that entity. Adoption of this section will expedite any future revisions to the forms incorporated under this section.

Post-Hearing Modification

Sections 11-406(a) through 11-406(f)

Specific Purpose/Factual Basis:

These sections are adopted but reserved for future use.

Post-Hearing Modification

Section 11-406(g)(1)

Specific Purpose:

This section is adopted to provide information on the Group Home Program Cost Report (SR 3).

The Department is incorporating by reference, pursuant to the California Code of Regulations, Title 1, Chapter 1, Section 20, the SR 3. This form is not printed in the California Code of Regulations or the Department's Manual of Policies and Procedures, because it would be cumbersome and impractical. However, this form is available during the 15-day public comment period from the Department by mail, fax or on the Department's web site.

Factual Basis:

Adoption of this section is necessary to specify that the SR 3 is a regulatory form used by a non-profit corporation to collect cost information for a specific group home program.

Final Modification

The SR 3 has been amended to capture cost data based on the group home program's "fiscal year," rather than a "calendar year." This modification was necessary for clarity and consistency with the financial audit report's reporting timeframes. As such, the revision date to the SR 3 has also been changed to December 2002, which will be reflected as 12/02 on the SR 3.

Post-Hearing Modification

Section 11-406(g)(2)

Specific Purpose:

This section is adopted to provide information on the Group Home Program Days of Care Schedule (SR 5).

The Department is incorporating by reference, pursuant to the California Code of Regulations, Title 1, Chapter 1, Section 20, the SR 5. This form is not printed in the California Code of Regulations or the Department's Manual of Policies and Procedures, because it would be cumbersome and impractical. However, this form is available during the 15-day public comment period from the Department by mail, fax or on the Department's web site.

Factual Basis:

Adoption of this section is necessary to specify that the SR 5 is a regulatory form used by a non-profit corporation to report historical or projected monthly data on occupancy and licensed capacity for a specific group home program.

Post-Hearing Modification

Section 11-406(g)(3)

Specific Purpose:

This section is adopted to provide information on the Group Home Program Payroll and Fringe Benefit Report (SR 4).

The Department is incorporating by reference, pursuant to the California Code of Regulations, Title 1, Chapter 1, Section 20, the SR 4. This form is not printed in the California Code of Regulations or the Department's Manual of Policies and Procedures, because it would be cumbersome and impractical. However, these forms are available during the 15-day public comment period from the Department by mail, fax or on the Department's web site.

Factual Basis:

Adoption of this section is necessary to specify that the SR 4 is a regulatory form used by a non-profit corporation to report historical or projected data on payroll and fringe benefits for a specific group home program.

Final Modification

The SR 4 has been amended to capture data based on a group home program's "fiscal year," rather than a "calendar year." This modification was necessary for clarity and consistency with the financial audit report's reporting timeframes. As such, the revision date to the SR 4 has also been changed to December 2002, which will be reflected as 12/02 on the SR 4.

Post-Hearing Modification

Section 11-406(g)(4)

Specific Purpose:

This section is adopted to provide information on the Group Home Program Rate Application (SR 1).

The Department is incorporating by reference, pursuant to the California Code of Regulations, Title 1, Chapter 1, Section 20, the SR 1. This form is not printed in the California Code of Regulations or the Department's Manual of Policies and Procedures, because it would be cumbersome and impractical. However, this form is available during the 15-day public comment period from the Department by mail, fax or on the Department's web site.

Factual Basis:

Adoption of this section is necessary to specify that the SR 1 is a regulatory form used by a non-profit corporation to apply for a group home program rate.

Post-Hearing Modification

Sections 11-406(h) through (o)

Specific Purpose/Factual Basis:

These sections are adopted but reserved for future use.

Post-Hearing Modification

Section 11-406(p)(1)

Specific Purpose:

This section is adopted to provide information on the Program Classification Report (SR 2).

The Department is incorporating by reference, pursuant to the California Code of Regulations, Title 1, Chapter 1, Section 20, the SR 2. This form is not printed in the California Code of Regulations or the Department's Manual of Policies and Procedures, because it would be cumbersome and impractical. However, this form is available during the 15-day public comment period from the Department by mail, fax or on the Department's web site.

Factual Basis:

Adoption of this section is necessary to specify that the SR 2 is a regulatory form used by a non-profit corporation to report historical or projected monthly data, which is used to establish a rate classification level (RCL) for a specific group home program.

Post-Hearing Modification

Sections 11-406(q) through (s)

Specific Purpose/Factual Basis:

These sections are adopted but reserved for future use.

Post-Hearing Modification

Section 11-406(t)(1)

Specific Purpose:

This section is adopted to provide information on the Total Program Cost Display (FCR 12FFA).

The Department is incorporating by reference, pursuant to the California Code of Regulations, Title 1, Chapter 1, Section 20, the FCR 12FFA. This form is not printed in the California Code of Regulations or the Department's Manual of Policies and Procedures, because it would be cumbersome and impractical. However, this form is available during the 15-day public comment period from the Department by mail, fax or on the Department's web site.

Factual Basis:

Adoption of this new section is necessary to specify that the FCR 12FFA is a regulatory form used by a non-profit corporation to collect cost information for a specific foster family agency program.

Final Modification

The FCR 12FFA has been amended to capture data based on a foster family home program's "fiscal year," rather than a "calendar year." This modification was necessary for clarity and consistency with the financial audit report's reporting timeframes. As such, the revision date to the FCR 12FFA has also been changed to December 2002, which will be reflected as 12/02 on the FCR 12FFA.

Post-Hearing Modification

Sections 11-406(u) through (z)

Specific Purpose/Factual Basis:

These new sections are adopted but reserved for future use.

b) Identification of Documents Upon Which Department is Relying

Public Laws 98-502 and 104-156

Department of Health and Human Services, Administration for Children & Families letter dated April 19, 2001.

Office of Management and Budget (OMB) Circular A-122, Cost Principles for Non-Profit Organizations

OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations

Government Auditing Standards of the Comptroller General of the United States (Yellow Book)

c) Local Mandate Statement

These regulations do not impose a mandate on local agencies or school districts. There are no state mandated local costs in these regulations which require state reimbursement under Section 17500, et seq. of the Government Code.

d) Statement of Alternatives Considered

CDSS has determined that no reasonable alternative considered or that has otherwise been identified and brought to the attention of CDSS would be more effective in carrying out the purpose for which the regulations are proposed or would be as effective and less burdensome to affected private persons than the proposed action.

e) Significant Adverse Economic Impact On Business

CDSS has made an initial determination that the proposed action will not have a significant, statewide adverse economic impact directly affecting businesses, including the ability of California businesses to compete with businesses in other states.

f) Testimony and Response

These regulations were considered at the Department's public hearings held on January 15 and 16, 2002. Oral testimony was presented by Debra Rose (Rose), Carol Carr (Carr), and Ritch North (North). Written testimony was received from Tahoe Turning Point (TTP), Ladonna Toliver (Toliver), California Alliance (Alliance) and Jeff Marks (Marks).

General Comments

1. Comment:

"Yes. Hello. My name is Debra Rose. I am the executive director of the California Association of Children's Facilities. We represent group homes and foster family agencies throughout California.

"I am here to talk about my concerns about the regulations concerning the OMB Circular A-133 and A-122. It is my belief that there are more questions that have not been addressed than there are answers before these regulations can be implemented. Questions as, you know, will the Department seek statutory change in law? If you start imposing the A-122 circular, that means that you will have to go to a cost base reimbursement system rather than the current aggregated capitated rate classification system. Are you going to change the Welfare and Institutions Code to reflect those type of changes? And how are you going to implement those changes? What kind of structure are you going to put in place? Are you going to go and speak to the Legislature about these changes?

"A second concern is training. The A-133 audit is a complicated audit. It has many different features. Right now what happens many times in the field with either community care licensing staff and foster rate staff is there's a lot of subjectivity. Without proper training how are you going to cross that bridge between community care licensing and their program analysts understanding how an A-133 procedure is to take place and how are you going to make that change with your own foster care rates auditors? Right now there is a lot of complications and a lot of subjectivity and a lot of problems. How are you gonna do all that training and what's the time frame? What is the time frame for all of your people in the field in training and do you have funding for that training?

"Second of all, it is not clear in the regulations, even though they say they're supposed to be implemented by July 1 of 2002, when and for what fiscal year are you going to make the A-133 audits effective? And you have to give enough notice to group home owners and foster family agencies when and how they are to comply. What about the manual that they have spoken about? When are you gonna have the audits manual ready? Are you gonna have it ready in time to do proper training not only of Department of Social Services staff but as well as the group home licensees and foster family agency licensees? This is a question that must be addressed. How are you going to handle anyone who has overpayment issues at the current time? That's another issue that has to be addressed. Are you going to have some sort of a phase-in system? What isn't allowable in an unallowable cost? Do you have to create statute to create allowable and unallowable costs? How specific are you going to have that list and who is gonna have input in developing that list?

"So these are the concerns that my association has in response to implementing A-133. Thank you very much and I look forward to your comments." (Rose)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. The regulation package was initiated as a result of a directive from the federal Department of Health and Human Services (DHHS), and to prevent loss of federal financial participation. Since release of the regulation package, The Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed.

Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received. The Department will issue a re-notice and make the revised regulation package available for comment.

In response to the comments regarding the complexity of the A-133 audits, consistency of application, and training, the providers' independent accountants will follow uniform industry standards in performing these audits. Providers should ensure that they contract with accountants who are knowledgeable of and experienced with OMB Circular A-133 audit requirements. The Department plans to provide technical assistance workshops for providers and their accountants when the audit guide is completed in the Spring of 2003. The Department staff will be involved in reviewing the completed audit reports rather than conducting the audits and will receive ongoing training on OMB Circular A-133 audit requirements. In addition, the regulations have been amended to ensure that they do not take effect until the provider has sufficient time to comply with the new regulations.

2. Comment:

"Good morning. My name is Carol Carr. I'm the executive director for Rubican Children's Center in Fremont, California. We operate five group homes. We service 30 children. We have been in existence for 30 years.

"In moving forward, my concerns are with the OMB circular A-133 and the A-122, and from an administrative perspective as the executive director, it really is unclear to me what the ask is of 133. What is it exactly that I need to prepare for? And specifically what is to determine allowable and unallowable costs because that's gonna drive the whole way that I process my whole financial system internally? How will this impact the agency in the day-to-day operations? What is my reporting structure to be able to comply with the A-133? What are the changes that i need to prepare for prior to the deployment of A-133 audit and the 122 guidelines? What is it that I will have to do from an employee perspective of staffing myself to make sure that I maintain compliance or that I am in compliance and are the additional software packages or whatever in the way that I operate my day-to-day operations?

"In light of the ongoing issues with the inconsistent interpretation of title 22 from the community care licensing analyst and that, what is the plan for training of the analysts so that there's some uniformity in the way that they interpret it whenever they come forward to conduct their audits? And what is the plan for funding? Where's the money that's going to come from for the training not only for the analysts but for the field staff and also for the individual agencies that are affected by the interpretations of the A-133? And in addition to that, is the Department of Social Services prepared to make the appropriate changes to their current rate classification level in order to adapt to the requirements of the A-133?

"In summary my question, which I really get to the true heart of why we have group homes and why we're in existence, is how does this bill truly benefit the safety, security and welfare of the children that we're servicing? Thank you." (Carr)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. The regulation package was initiated as a result of a directive from the federal DHHS, and to prevent loss of federal financial participation. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received. The Department will issue a re-notice and make the revised regulation package available for comment.

In response to the comments on training and consistency of application for the A-133 audits, the providers' independent accountants will follow uniform industry standards in performing these audits. Providers must ensure that they contract with accountants who are knowledgeable of and experienced with OMB Circular A-133 audit requirements. The Department plans to provide technical assistance workshops for providers and their accountants when the audit guide is completed in the spring of 2003. The Department staff will be involved in reviewing the completed audit reports rather than conducting the audits and will receive ongoing training on OMB Circular A-133 audit requirements.

3. Comment:

"My name is Ritch North. I'm the administrator of North Valley Children & Family Services, a foster agency and based in Chico. I also represent the Association for Better Children Services. It's an association of foster agencies in the north valley, north of Sacramento.

"Our concerns are on clarity, the confusion of the changes, the proposed changes the system appears to be making. Our concerns are what is the time line? We don't have objection to change. We certainly aren't trying to keep away from being held

accountable to the expenditure of the funds. It does seem to mean a major change in how we do business, for example, allowable versus unallowable costs being held to A-133. It has been mentioned already the training, training alone, training for the auditors, training for our agencies to be able to comply changing how we do business. Yes, what year will begin our accountability to this major change? Also we have questions about the cost reimbursement system versus the way it is now, which is a capitated rate. How do you -- what does this mean? How do you hold -- how do you have a capitated rate and be held to the allowable/unallowable in A-133? We just have a lot of questions and are really concerned about when we will have a better understanding. And how is the state gonna pull this off? It just feels like a major change. And those are the extent of my unprepared comments." (North)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. The regulation package was initiated as a result of a directive from the federal DHHS, and to prevent loss of federal financial participation. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received. The Department will issue a re-notice and make the revised regulation package available for comment.

In response to the comments regarding the complexity of the A-133 audits, consistency of application, training, and implementation timelines, the providers' independent accountants will follow uniform industry standards in performing these audits. Providers should ensure that they contract with accountants who are knowledgeable of and experienced with OMB Circular A-133 audit requirements. The Department plans to provide technical assistance workshops for providers and their accountants when the audit guide is completed in the Spring of 2003. The Department staff will be involved in reviewing the completed audit reports rather than conducting the audits, and will receive ongoing training on the appropriate audit elements. In addition, the regulations have been amended to

ensure that they do not take effect until the provider has sufficient time to comply with the new regulations.

4. Comment:

"As the regulatory foundation of Chapter 11-400 AFDC - Foster Care Rates (FCR 11-400) is expended to include Management and Budget Circular A-122, a-133 and other federal legislation, it is imperative that the language of 11-400 be expanded and clarified through similar public hearings. Specific sections addressed in this opinion include, but is not limited to sections 11-400r.(3), 11-402.636, 11-402.82, and 11-405.13. These sections relate to the concept of nonallowable costs, allowable cost categories, and Circular A-122." (TTP)

Response:

The Department thanks the testifier for their comments. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received**.** The Department will issue a re-notice and make the revised regulation package available for public comment.

5. Comment:

"Item one.

"Circular A-122 addresses administrative caps. Currently, it appears that administrative expenses over 26% will be nonallowable. Past discussions with Foster Care Rates have identified administrative expenses at or under 18% as reasonable. To my knowledge, there is no definition in FCR 11-400 relating to the allowable percent of administration." (TTP)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input

into development of the OMB Circular A-133 regulations. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received. The Department will issue a re-notice and make the revised regulation package available for comment.

6. Comment:

"Item two

"Attachment B of Circular A-122, paragraph 11 states that, "c. The computation of use allowances or depreciation will exclude: (1) The cost of land; (2) Any portion of the cost of buildings and equipment borne by or donated by the Federal Government irrespective of where title was originally vested or where it presently resides; and (3) Any portion of the cost of buildings and equipment contributed by or for the organization in satisfaction of a statutory matching requirement."

"It appears that for providers that own or making payments on buildings and lands, all AFDC-FC funds that relate to (1), (2) or (3) above are nonallowable and must be accounted for and returned. This issue needs to be addressed in FCR 11-400." (TTP)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the

Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received. The Department will issue a re-notice and make the revised regulation package available for comment.

7. Comment:

"Item three

"Attachment B of Circular A-122, paragraph 15 states that, "b. (1) Capital expenditures for general purpose equipment are unallowable as a direct cost except with the prior approval of the awarding agency. (2) Capital expenditures for special purpose equipment are allowable as direct costs, provided that items with a unit cost of $5000 or more have the prior approval of awarding agency. c. Capital expenditures for land or buildings are unallowable as a direct cost except with the prior approval of the awarding agency. d. Capital expenditures for improvements to land, buildings, or equipment which materially increase their value or useful life are unallowable as a direct cost except with the prior approval of the awarding."

"To protect the well-being of the foster children in California to prevent the disallowance of these legitimate expenses, FCR 11-400 needs to address procedures for prior approval." (TTP)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, The Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received**.** The Department will issue a re-notice and make the revised regulation package available for comment.

8. Comment:

"Item four

"Attachment B of Circular A-122, paragraph 16 states that, "Costs of fines and penalties resulting from violations of, or failure of the organization to comply with Federal, State, and local laws and regulations are unallowable except when incurred as a result of compliance with specific provisions of an award or instructions in writing from the awarding agency."

"Given that penalties assessed by CCL are non allowable, must providers both pay the fine and refund the same amount as an nonallowable cost?" (TTP)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received. The Department will issue a re-notice and make the revised regulation package available for comment.

9. Comment:

"Item five

"Attachment B of Circular A-122, paragraph 23 states that, "(i) Interest on debt incurred to finance or refinance assets acquired before or reacquired after the effective date of this Circular is not allowable.... However, interest on debt incurred after the effective date of this revision to acquire or replace capital assets (including renovations, alterations, equipment, land, and capital assets acquired through capital leases), acquired after the effective date of this revision and used in support of sponsored agreements is allowable"

"In that the date of this circular is June 1, 1998, is it true that foster children residing in homes with mortgages to provider agencies initiated prior to June 1, 1998 must be uprooted, the homes sold, and the children's life disrupted? This sounds like a great foundation for a suit." (TTP)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, the CDSS has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received. The Department will issue a re-notice and make the revised regulation package available for comment.

10. Comment:

"Item five

"Attachment B of Circular A-122, paragraph 32 states that, "Premiums for overtime, extra-pay shifts, and multi-shift work are allowable only with the prior approval of the awarding agency..."

"In our agency, we utilize a 54 hour week, which included 14 hours of overtime, to minimize the care providers for the foster children in our care and to maximize the opportunity for those children to gain attachments to positive adult role models. FCR 100-400 will need to develop a mechanism for prior approval before auditors identify nonallowable overtime costs." (TTP)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, the Department has received additional clarification of the

audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received. The Department will issue a re-notice and make the revised regulation package available for comment.

11. Comment:

"Attachment B of Circular A-122, paragraph 46 states that, "c. Rental costs under less-than-arms length leases are allowable only up to the amount that would be allowed had title to the property vested in the organization. For this purpose, a less-than-arms-length lease is one under which one party to the lease agreement is able to control or substantially influence the actions of the other. Such leases include, but are not limited to those between (i) divisions of an organization; (ii) organizations under common control through common officers, directors, or members; and (iii) an organization and a director, trustee, officer, or key employee of the organization or his immediate family either directly or through corporations, trusts, or similar arrangements in which they hold a controlling interest."

"Currently, FCR 11-400 and the Attorney General identifies only corporate board members as being interested partied to affiliated leases. Regulations need to be rewritten to parallel the language in Circular A-122." (TTP)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for

which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received. The Department will issue a re-notice and make the revised regulation package available for comment.

12. Comment:

"I am writing to voice our my concerns regarding the new audit requirements for group homes. I have just been told by another provider that there was a hearing this morning for the public to make comments in Sacramento. I would have wanted to be there on behalf of our facility and the children that we serve.

"I just want to say that I understand the intent of the audit requirements and I fully support that group homes be accountable for the funds that are received on behalf of children. I do not understand why small group homes have to absorb so much of the costs associated with the audit. My husband and myself started our home 6 years ago and it is very rewarding and very challenging work. I cannot understand how a study was conducted to determine that a small 6 bed facility could possibly afford the increasing costs of the audit. In fact we along with 7 other facilities had recently asked our county (Alameda) for emergency funding support.

"The costs of our first audit was $6000 and the one last year was $3000. We received half back to help defray the costs, but the is still and extreme hardship for our budget. Over the last 2 years we have had to drastically increase our salaries for line employees in order to retain quality staff. The increases over the last 3 years have not kept up with this inflationary costs. Also our workers compensation and liability insurance has risen more than 150%. We pay over $2200 each month just for insurance. The reason that I am stating this is to express my fears that as these audit costs continue to impact 6 bed facilities then this will destroy our budget. Costs are already trimmed to the bone and the sources that will continue to be hit will be Care and supervision which is a direct influence to the kind of care that our kids deserve. Currently the firm that did the audit last year have stated that the cost will likely double or more.

"Please help keep costs reasonable and review the actual budget for 6 bed facilities and you will find that the intent of 933 did not include taking away vital programs and quality supervision for children. Please advise me who I can also email for support. There has to be an alternative for these audit costs. Maybe smaller facilities can continue with the GASA audit or maybe there can be random audits or some other way to stop taking away critical funding for the effective treatment for our children." (Toliver)

Response:

The Department thanks the testifier for their comments and understands the testifier's concern regarding audit costs for small group homes. However, reimbursement to providers for the cost of the required financial audit is capped by statute as specified in Welfare and Institutions Code Section 11466.21(c). The OMB Circular A-133 audit requirements only apply to corporations expending $300,000 or more in combined federal funds. Therefore, the Department does not anticipate the audit costs for small 6-bed facilities to increase significantly, as most of them are exempt from the OMB Circular A-133 audit requirements due to the funding threshold. These providers would continue to submit the generally accepted government auditing standards (GAGAS) audit.

13. Comment:

"I am the administrator of Green Pastures, Inc. a six bed group home for both DSS and DDS children. Our auditor tells me that if we are required to comply with this more stringent government audit for federal funds, that it is your responsibility to define how much of our gov't income is federal and provide a CFDA (Catalog For Domestic Assistance) number.

"Please let me know our status on this so that we can move forward on this year's audit procedure." (Marks)

Response:

The Department thanks the testifier for their comments. The testifier is correct in noting that the determination of total federal funds received by a provider is critical in establishing whether an A-133 audit is required. As such, the Department will be issuing instructions to providers for determining the portion of funds received from the counties that were federal Title IV-E funded.

Necessity, Authority and Consistency

14. Comment:

"A. Necessity

"Before responding to the individual sections proposed for adoption in the noticed regulations, we have preliminary objections to the adoption of the package because its scope far exceeds the events which preceded its adoption. Thus, there is no "necessity" for adoption of this regulation package. The regulatory Notice and the Initial Statement of Reasons reference a letter dated April 3, 2001 from the DHHS, Administration for Children and Families (ACF) and an April 19, 2001 letter from DHHS**,** ACF, regarding the federal government's preliminary decision that group homes and foster family agency providers are not vendors and

are subrecipients of federal funds. First, it is our understanding that is a preliminary, not a final, decision and that Region IX is further researching its preliminary decision and may change the outcome. If the federal government, after review of its preliminary decision, concludes that group homes and foster family agencies are vendors and not subrecipients - which has been the prevailing rule for in excess of 10 years - there is no need to adopt regulations implementing OMB A-133 audit requirements. A copy of the Federal Single Audit Act and OMB A- 133 are attached as Exhibit "1."

"Attached hereto as Exhibit "2" and incorporated herein by this reference is a letter dated December 7, 2001 to Ms. Sharon Fujii, Region IX Director, from Sylvia Pizzini, the Deputy Director of Children and Family Services Division. The third paragraph of that letter requests further comments regarding the criteria for vendors and subrecipients contained in section .210 of OMB Circular A-133. Attached hereto as Exhibit "3" and incorporated herein by this reference is a copy of a letter dated December 20, 2001 from Sylvia Pizzini and Carroll Schroeder to Ms. Sharon Fujii discussing the vendor/subrecipient issue and seeking further direction regarding the issue.

"In California, the current rate statutes took effect in July 1990, and the group home and foster family agency rate setting regulations implementing those statutes, contained in MPP sections 11-400, 11-402 and 11-403, for over 10 years have been based upon state determinations that group homes providing residential services to AFDC-FC eligible children and foster family agencies providing residential care and supervision to AFDC-FC eligible children are "vendors." Attached hereto as Exhibit "4" and incorporated herein by this reference is a letter issued by the Department of Social Services in 1997 which determines that group homes and foster family agencies are vendors under the then applicable OMB A-133 criteria. For at least the last 10 years, both the Department of Social Services and the California Alliance members have operated under the Department of Social Services determination that they were vendors of services and not subject to various provisions of the Federal Single Audit Act (31 U.S.C. § 7501 et seq.) that required OMB A-133 audits. Thus, the April 2001 letters from Region IX came as a surprise regarding the decision that group homes and foster family agencies are "subrecipients."

"There are multiple consequences to the Region IX preliminary decision regarding subrecipient status, some of which raise fundamental inconsistencies with the California rate setting system and the statutory and regulatory provisions that define the rate setting system. The threshold question is whether it is now necessary to adopt the regulations. In short, there is no substantial evidence in the record that demonstrates the need for this regulation. There is a preliminary federal decision reversing in excess of 10 years of practice and understanding. There have been no statutory changes to the rate setting system that would justify or warrant this change. We submit these regulations are not necessary until such time as a final decision is made by the Director of the Office of Management and

Budget. Under the Federal Single Audit Act, the Director of the Office of Management and Budget is vested with the authority to provide "guidance" regarding vendor status (31 U.S.C. § 7501(a)(5). If the Director of the Office of Management and Budget finally decides that California group homes and California foster family agencies are subrecipients and subject to the OMB A-133 audit requirements, then that system may be implemented either by statute or regulation in California if and when it occurs.

"In the only reported judicial decision discussing the current rate setting system in California, the Court described the group home there involved as a "vendor." In *Sacramento Children's Home v. State Department of Social Services* (2000) 81 Cal.App. 4th 786, starting at page 789, the Court consistently refers to the group home as a "vendor." Attached as Exhibit "5" is a copy of the Court's decision. That characterization certainly reflects the understanding of the Department, the vendor community, and the courts regarding the status of the group home provider under the capitated or flat-rate system.

"Alternatively, the California Alliance believes that under the necessity criterion, these regulations could simply mandate the implementation of OMB A-133 audits. That would be directly responsive to the preliminary determination of Region IX. The scope and reach of the regulations, however, are far broader. They fundamentally change the capitated rate setting system by transposing cost reimbursement principles from a state-claiming issue to a provider "eligibility" issue without any change in the state authorizing legislation; they propose to collect overpayments based on OMB A-133 management decisions which have historically been state and federal government claiming issues; and they propose to collect overpayments based upon expenditures that are unallowable or unreasonable or not "actual" pursuant to the provisions of OMB A-122. To the extent that the proposed regulations go beyond implementation of OMB A-133 audits, they violate the necessity criterion in the Administrative Procedure Act." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients, and therefore subject to OMB Circular A-133 audit requirements. In order to protect and preserve California's eligibility for federal financial participation under Title IV-E, the Department has determined that regulations implementing OMB Circular A-133 are necessary.

As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, The Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received. The Department will issue a re-notice and make the revised regulation package available for comment.

15. Comment:

"B. Authority

"The California Alliance also objects to the adoption of this regulation package on the basis that the Department does not have the "authority" to adopt this package. The Notice of Proposed Changes references Welfare and Institutions Code section 11466.21 on the grounds that the Department was informed "that the type of audit California has required under Welfare and Institutions Code section 11466.21 does not meet the federal audit standard as required under federal OMB Circular A-133. Exhibit "6" attached is a true and correct copy of Welfare and Institutions Code section 11466.21. That section was added to the Welfare and Institutions Code by the Legislature in 1998. Significantly, it does not, by its terms, require an OMB A-133 audit; it merely requires a "financial audit."

"Welfare and Institutions Code section 11466.21(a)(4) states:

"The provider shall have its financial audits made using generally accepted accounting standards applicable to private entities organized and operated on a nonprofit basis.

"That language, we believe, mandates financial audits pursuant to "generally accepted auditing standards applicable to ..." nonprofits. Those are known as AICPA (American Institute of Certified Public Accountants) standards which are different audit standards than OMB A-133 audit standards. In short, these regulations require different audit standards than those specified in the statute and thus create an impermissible inconsistency with Section 11466.21(a)(4).

"In 1998, the Legislature passed and adopted Welfare and Institutions Code section 11466.21 and the Department of Social Services implemented it by regulation requiring non-OMB A-133 audits. This proposed change, however, without any change in the statute, significantly changes the scope and cost of the audits by the requirement for non-profit corporations who expend $300,000 or more in combined federal funds on all of their programs and activities during a

fiscal year. Generally speaking, the federal government funds approximately one-third of the cost of providing residential and foster family agency services to eligible AFDC-FC children. Thus, the $300,000 limit will apply to any group home or foster family agency with a budget in excess of $900,000 annually. That will apply to the vast majority of group homes and foster family agencies in California.

"Welfare and Institutions Code section 11466.21 provides an eligible provider (12 beds or less) will receive up to $2,500 annually to offset the audit cost mandated by the Legislature in 1998. OMB A-133 audits are much more expensive than current audits because of the requirements in OMB A-133 for compliance testing which covers, in the case of Title IV-E funds, 10 different compliance tests. The applicable CFDA for Title IV-E is 93.658. Attached hereto as Exhibit "7" is a copy of the CFDA 93.658 statement for compliance testing, the A-133 compliance supplement, and the OMB A-133 Internal Control and Subrecipient Monitoring Supplement. The compliance testing requirements are what distinguish OMB A-133 audits from non-A-133 audits. The California Alliance estimates that A-133 compliance testing will add an average of $2,000 to $10,000 per audit to the cost of current audits, depending on the size of the provider and the complexity of programs and sources of funding. Clearly, the Legislature never contemplated the implementation of this requirement and certainly does not reimburse group homes and foster family agencies for the additional costs incurred.

"In summary, absent a legislative change authorizing OMB A-133 audits and increasing the reimbursement for the cost of the OMB A-133 audits, the Department is exceeding the authority contained in Welfare and Institutions Code section 11466.21 to implement these regulations." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, The Department has received additional clarification of the audit requirements from the federal DHHS and confirmation that non-profit corporations operating group homes and/or foster family agencies are deemed subrecipients. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulation package.

Due to California's capitated flat-rate system, and the February 22, 2002 federal letter, which narrows the scope of the A-133 audits, OMB Circular A-122 Cost Principles will not be applied to group home or FFA providers. Consequently, the number of applicable Title IV-E compliance supplements requirements will be reduced considerably.

In addition, the OMB Circular A-133 audit requirements only apply to corporations expending $300,000 or more in combined federal funds, as such, we do not anticipate that audit costs for small, 6-bed facilities will increase significantly as most of these programs would likely be exempt from the OMB Circular A-133 audit requirement. These providers would continue to submit the GAGAS audit. The increased costs of the OMB Circular A-133 audit for affected providers is expected to range between $1,500 and $2,500 when performed by an experienced certified public accountant (CPA). Since, reimbursement to eligible providers for the cost of the required financial audit is authorized and capped by statute as specified in Welfare and Institutions Code Section 11466.21(c), no additional reimbursement can be authorized in regulation.

The testifier correctly notes that state statute at Welfare and Institutions Code Section 11466.21 does not specify the audit standard to be applied to the financial audit. This makes it necessary for the Department through regulations to establish the appropriate audit standard that complies with federal law. The Department has authority under Welfare and Institution Code Sections 10553 and 10554 to formulate and adopt regulations. Welfare and Institutions Code Section 11460 designates the CDSS as the single organizational unit whose duty is to administer a state program for establishing foster care rates. Welfare and Institutions Code Section 11461.5 authorizes the Department to develop regulations concerning group home rates. Welfare and Institutions Code Section 11463 authorizes the Department to develop a rate system for FFAs and to develop regulations concerning FFAs. Finally, because federal law and regulation supercede state law or regulation, California must adhere to all federal requirements in order to prevent the loss of federal financial participation in the foster care program. The Department will issue a re-notice and make the revised regulation package available for comment.

16. Comment:

"C. Consistency

"The California Alliance also objects to this regulatory package on the grounds that it violates the "consistency requirement" in that it is not in harmony with, and not in compliance with, existing statutes and other provisions of law. We have already explained why the implementation of the OMB A-133 audit requirement violates Welfare and Institutions Code section 11466.21, both in terms of the type of audit and the cost reimbursement provisions. However, the inconsistency created by the adoption of this regulatory package is far broader than the issue of financial audits pursuant to Welfare and Institutions Code section 11466.21.

"In California, the statutory rate setting provisions for group homes are contained in Welfare and Institutions Code section 11462, et seq. That statute mandates payment of a standardized schedule of rates contained in section 11462(f). This

has been known since its inception in 1990 as a flat rate or "capitated" system. For example, a group home classified at rate classification level (RCL) 10 receives $4,064 per month per child. The amount the group home expends to provide the required level of care and services for this child is not even statutorily identified or recognized. The group home provider is required to maintain services consistent with the established rate classification level based upon the point system contained in Welfare and Institutions Code section 11462(f). In other words, for an RCL 10, they must deliver an average of at least 300 points during the 12-month period for which the rate is set. Those points are audited not by fiscal audits, but by "program audits" pursuant to Welfare and Institutions Code section 11466.2. The program audits referenced in Welfare and Institutions Code section 11466.2 are completely separate and autonomous audits from financial audits under current standards or fiscal audits under OMB A-133 standards. Program audits monitor points, not financial or fiscal accounting procedures.

"This regulatory package, however, proposes to fundamentally change the system of paying for group home services from a capitated. system to a cost-based system that incorporates federal cost reimbursement principals, but will not reimburse providers for all of their actual allowable and reasonable costs. In effect, the current schedule of standardized rates would be transformed into a schedule of rate maximums. These proposed regulations do that by making federal allowability standards a precondition to eligibility and by the generation of overpayments to reimburse the state for items of cost reimbursement that are not "allowable" or "reasonable" or not "actual." Individual objections to the sections that adopt these regulatory changes will later be identified.

"There has been no change in the statutory rate setting provisions. The applicable statutory provisions still provide for a capitated system, but these regulations propose to reduce those levels, both through eligibility determinations and through recovery of overpayments associated with OMB A-133 audits and fiscal overpayments based upon the application of OMB A-133/A-122 audits. It is the California Alliance's opinion that, absent statutory changes, this regulatory package lacks authority and is not consistent with state statutes regarding rate setting because it fundamentally changes the system to a cost or quasi-cost reimbursement system.

"To further understand how fundamentally these regulations propose to change the rate setting system without statutory authorization, the California Alliance directs your attention to the Department's Administrative Standards for Eligibility and Assistance Programs - AFDC-Foster Care Rates - commencing in MPP section 11-400. Essentially, the rate classification point system is based upon the accumulation of the aggregate points associated with the provision of three functions: child care and supervision, social work, and mental health. In a typical group home rate application it is not unusual for approximately 80% of the points to be generated by child care and supervision, a federally allowable cost; 10% - 15% of the points generated by social work activities providing social work

services to children, a federally unallowable cost but an allowable state cost; and 5% - 10% of the points being generated by mental health activities, an unallowable cost both for state and federal purposes. In other words, for a group home to generate the necessary points it must generate approximately 20% of its points on the basis of federally unallowable costs. With the implementation of these regulations, the State of California proposes to collect from group home providers federally unallowable costs - expenditures which are mandated in order to achieve points under the rate setting system.

"Historically, the issue of recovery of unallowable costs from group home providers has not been an issue under the capitated or flat rate system, provided the requisite number of points or services are generated for the children. It has historically been a claiming issue as between the state government and the federal government; that is, California has decided to incur costs on behalf of children in group homes for social work activities and reimburse providers for them even though they are federally unallowable. This regulatory package states for the first time that the state intends to recoup those federally unallowable costs from group homes. Again, we respectfully submit that is a fundamental change in the rate setting system which is not authorized by Welfare and Institutions Code section 11462 and is inconsistent with Welfare and Institutions Code section 11462, which continues to contain the capitated or flat-rate system for reimbursement for services.

"In the event that the preliminary Region IX determination prevails, and a final determination is made that group homes and foster family agencies in California must be treated as "subrecipients" and obtain annual A-133 audits, the California Alliance believes that the Department has two basic options. Under the first option, the Department can (a) retain its current capitated payment system for group homes and foster family agencies; (b) require these providers to obtain A-133 audits; (c) use the results of those audits to identify federal Title IV-E funds that have been expended for costs that do not fall under the federal definition of "allowable" costs; and (d) reduce the state's claim for federal Title IV-E reimbursement to reflect the amount spent to pay for federally-defined "unallowable" costs. Under the second option, the Department can seek statutory authority from the State Legislature to eliminate its current capitated rate-setting systems and to establish a new system for establishing AFDC-FC rates for group homes and foster family agencies based on cost reimbursement principles. Under a cost reimbursement system, (a) each group home and foster family agency would be paid a rate that would cover its actual, allowable, and reasonable costs; (b) annual A-133 audits would then be used as the basis for a financial reconciliation between the provider and the counties, with the provider repaying any AFDC-FC funds not spent for allowable costs or the counties making supplemental payments to pay for any allowable cost not covered by previous payments; and (c) the A-133 audits would also be used by the counties to adjust their AFDC-FC claim to the Department, which would then adjust its claim for federal Title IV-E reimbursement to reflect the actual amount spent to pay for

federally-defined "allowable and reasonable" costs. However, until and unless the State Legislature acts to create a new AFDC-FC rate-setting system, the California Alliance believes that the first option is the only option available to the Department at this time." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients, and therefore subject to OMB Circular A-133 audit requirements. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received. The Department will issue a re-notice and make the revised regulation package available for comment.

Cost Estimate/Local Mandate Statement and Small Business Impact

17. Comment:

"The Department's Notice of Proposed Changes in Regulations contains a cost estimate which disclaims any fiscal impact to any state agency or program. The California Alliance disagrees. If the State of California, through these regulations transforms the rate system from a capitated or flat-rate system to a cost reimbursement system, there are substantial economic impacts to the State of California. One of the primary reasons for the adoption of the flat-rate system was cost containment. That is, providers would be paid a flat rate which was unrelated to their actual costs. If providers are now subjected to eligibility determinations based upon the expenditure of actual allowable and reasonable costs, subjected to potential overpayments based upon management decisions, and subjected to potential overpayments based upon OMB A-133/A-122 cost reimbursement principles, the conversion to an actual, allowable, and reasonable cost reimbursement system has a corollary impact on state agency programs. The California Alliance estimates that the group home residential care program is underfunded by approximately $60 million to $80 million per year. By transforming the system from a capitated system to a cost reimbursement system,

the state has potential exposure for additional payments based upon these cost reimbursement regulations. The cost estimate should identify this fiscal impact or potential fiscal impact.

"The Department's Notice of Proposed Changes also contains a local mandate disclaimer. The California Alliance disagrees. Specifically, the requirements of OMB Circular A-133 that require management decisions to be made by pass-through entities (.405(c)) has substantial cost impacts on counties since, under the OMB A-133 hierarchy, counties are the "pass -through entities." That is, counties must make OMB A-133 management decisions. Group homes and foster family agencies may render services to one, five, ten, or more different counties. While it is singularly unclear how counties will make management decisions, it is clear that the 58 counties in California have that obligation under both the Federal Single Audit Act and OMB A-133. That is a local government mandate in these regulations.

"We know, for example, that the County of Los Angeles contracts with between 200 and 250 different foster care providers. The County of Los Angeles will have to add staff to review all of the OMB A-133 audits for its providers. It then will need to make management decisions if the OMB A-133 audits disclose findings which may initiate management decisions. While we do not know the cost of this local mandate, it is very clear that such a mandate exists. Obviously, smaller counties that utilize fewer group homes and foster family agencies may require fewer staff, but there nevertheless is a mandate in these regulations which the state fails to recognize and, in fact, even erroneously disclaims.

"As the single state agency responsible for the federal Title IV-E AFDC-FC program in California, the Department of Social Services must ensure that the program is administered in a uniform and consistent manner throughout the state. Therefore, the Department must adopt regulations that govern how the counties will perform the "management decision" process and monitor county performance to ensure that the regulations are being followed in practice. These regulations will have to include provisions for the protest and appeal of a county "management decision" by a provider.

"The Small Business Statement in the Notice of Proposed Changes in Regulations indicates that there may be an economic impact on small businesses operating group homes or foster family agencies. It acknowledges that the more stringent audit requirements may require operating changes in fiscal reporting and higher audit fees. However, it fails to identify, and apparently either ignores or disclaims, the most obvious small business impact because of the imposition of an eligibility requirement as a precondition to the receipt of Title IV-E funds, the impact of overpayments based upon management decisions, and the impact of overpayments based upon the OMB A-122 cost reimbursement principles.

"As we argue in other provisions of this comment, to the extent that the state seeks to convert a flat rate or capitated system to a cost reimbursement system, it fundamentally changes the nature of the relationship. That change will necessarily change group home and foster family agency revenues and expenditures. While we cannot quantify the dollars involved, there will be changes to revenues and expenditures. The impact analysis fails to identify these small business impacts." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, the Department has received additional clarification of the audit requirements from the federal DHHS. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulation package.

While the definition of "pass-through" entities in OMB Circular A-133 may include counties, the "State established *rate system*" in California does not provide for a mutually exclusive relationship between the pass-through counties and their sub-recipients. Many of the sub-recipients receive placements and payments from more than one county at any given time making the counties' ability to act as the single pass-through entity for the audit and management decisions administratively cumbersome. Therefore, in order to simplify the process and to provide consistency, the Department will serve as the pass-through entity for purposes of the audit and management decisions.

With respect to the comment concerning the Small Business Impact Statement, this is a part of the Statement of Reasons which is included in all regulation packages as required by of Welfare and Institutions Code Section 11462.4. This section states that group homes and foster family agencies shall be deemed small businesses and the department shall project the impact on group homes and foster family agencies of any new regulations which will affect those community care facilities. The purpose is simply to determine if the proposed regulations will have an economic impact on small businesses. In this instance, "small business" is used generically to refer to small operations such as group homes, rather than as a legal definition of small businesses. In addition, Health and Safety Code Section 1566.3 specifically states that group homes of 6 beds or less are exempt from zoning ordinances. Nothing in this regulation package would affect that law. The CDSS will issue a re-notice and make the revised regulation package available for comment.

Small Business Impact Statement

18. "Item finally (sic)

"I have a major concern that you believe that small businesses are being addressed. If you are only concerned with small business, all group home providers need not be concerned with this hearing because none of us are small businesses.

"According to the SMALL BUSINESS IMPACT STATEMENT, "The CDSS finds these regulations may have an economic impact on small businesses operating group home programs or foster family agencies."

"Given that AFDC-FOSTER CARE RATES REGULATIONS Chapter 11-400 section 11-400g(2)(A) states "'Group Home' means a nondetentional privately operated residential home, organized and operated on a nonprofit basis only, of any capacity, that provides services in a group setting to children in need of care and supervision, as required by paragraph (1) of subdivision (a) of Section 1502 of the Health and Safety Code," only nonprofit organizations can be group homes. Small business can not provide group home services.

"California Health and Safety Code 1566.2 states, "A residential facility, which serves six or fewer persons shall not be subject to any business taxes, local registration fees, use permit fees, or other fees to which other single family dwellings are not likewise subject.

"California Health and Safety Code 1566.3 states, "Whether or not unrelated persons are living together, a residential facility which serves six or fewer persons shall be considered a residential use of property for the purposes of this article. In addition, the residents and operators of such a facility shall be considered a family for the purposes of any law or zoning ordinance which relates to the residential use of property pursuant to this article. For the purposes of all local ordinances, a residential facility which serves six or fewer persons shall not be included within the definition of a boarding house, rooming house, institution or home for the care of minors, the aged, or the mentally infirm, foster care home, guest home, rest home, sanitarium, mental hygiene home, or other similar term which implies that the residential facility is business run for profit or differs in any other way from a single family residence.... No conditional use permit, zoning variance, or other zoning clearance shall be required of a residential facility which serves six or fewer persons which is not required of a single family residence in the same zone."

"It is ill advised that the CDSS infer that those nonprofit organizations that operate group home program are small business. This can lead to grave consequences on two accounts. First, the concept that group homes can be operated as only a nonprofit basis can be severely undermined. Secondly, for group homes serving six or fewer children to be labeled as a small business sets the stage for communities and counties to enact zoning requirements for residential facilities, which serves six

or fewer persons, to be required the same zoning requirements of other similar small businesses.

"This, in turn, would open both the CDSS and others to be in potential violation of the California Fair Housing Act of 1992, which declares, as the public policy of California, that it is necessary to protect and safeguard the right and opportunity of all persons to seek, obtain, and hold employment without discrimination or abridgment on account of... familial status... Further, the practice of discrimination because of... familial status or disability in housing accommodations is declared to be against public policy... For purposes of this part, "familial status" means one or more individuals under 18 years of age who reside with a parent, another person with care and legal custody of that individual, a person who has been given care and custody of that individual by a state or local government agency that is responsible for the welfare of children.

"It is strongly recommended that you revise the language under the SMALL BUSINESS IMPACT STATEMENT to be identical to that which was used in the implementation of SB933 FOSTER CARE REFORM (ORD #1098-30) on January 4, 1999, and that of AB 1575 GROUP HOME PROGRAM - FOSTER CARE REGULATIONS (ORD #0898-25) which simply stated "CDSS has determined that there is no adverse impact on small businesses as a result of filing these regulations because these regulations do not affect small businesses." (TTP)

Response:

The Department thanks the testifier for their comments. The Small Business Impact Statement is a part of the Statement of Reasons included in all regulation packages as required by Welfare and Institutions Code Section 11462.4. This Section states that group homes and foster family agencies shall be deemed small businesses and the department shall project the impact on group homes and foster family agencies of any new regulations which will affect those community care facilities. The purpose is simply to determine if the proposed regulations will have an economic impact on small businesses. In this instance, "small business" is used generically to refer to small operations such as group homes, rather than as a legal definition of small businesses. In addition, Health and Safety Code Section 1566.3 specifically states that group homes of 6 beds or less are exempt from zoning ordinances. Nothing in this regulation package would affect that law.

Section 11-400f.(7)

19. Comment:

"The definition of a "fiscal audit" as proposed to be amended will include a "financial audit." Financial audits are, by statute and regulation, conducted by a certified public accountant or a state-licensed public accountant, not the

Department of Social Services. Fiscal audits are audits conducted by the Department. This regulation defines fiscal audits and financial audits as audits conducted by the Department of Social Services. At a minimum, this will create ambiguity and confusion and thus violates the "clarity" standard.

"The Initial Statement of Reasons identifies this amendment as necessary for clarity and consistency with Welfare and Institutions Code section 11466.2 for the recovery of sustained financial audit overpayments and to ensure that California meets federal audit standards for the foster care program as required by OMB Circular A-133 and also to ensure that Title IV-E federal financial participation in the program is not jeopardized. Actually, Welfare and Institutions Code section 11466.2 only provides for the recovery of overpayments "resulting from an overstatement of the projected level of care and services." This type of audit is a program audit. Significantly, the statutory provisions do not include either fiscal audits or financial audits.

"Because the statutory provisions only provide for the recovery of overpayments based upon an overstatement of the projected level of care and services as defined in the RCL point system and because the only audit modality that measures the projected level of care and services is the program audit, the Department is attempting to create an additional regulatory basis for the recovery of overpayments which exceeds the authorizing statute. The regulation, therefore, violates the statutory standards for authority, consistency and necessity." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. As a result of the input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. The Department has revised the definition of fiscal audit and deleted the reference to financial audit. Additionally, in the Final Statement of Reasons, the Department has corrected the reference to the Welfare and Institutions Code Section to 11466.2 et seq. With respect to the testifier's concerns regarding the Department's authority to collect overpayments, the legislature has in Welfare and Institutions Code Sections 11466.2 and 11466.21, authorized the Department to conduct or have conducted fiscal and financial audits. Implicit in this authority is the power to require remediation of findings made in those audits. Moreover, OMB Circular A-133 requires among other actions, recovery of unallowable costs. The Department will issue a re-notice and make the revised regulation package available for comment.

Section 11-400m.(4)

20. Comment:

"This section includes a definition of a "management decision." The definition, however, assigns the responsibility for the management decision to the Department of Social Services. That appears to be contrary to the provisions of OMB A-133. Under the applicable OMB A-133 provisions, the State of California is a "recipient." The counties are the pass-through entities. Pursuant to OMB A-133 subsection .405(c), the pass-through entities or, in California, the counties, are to be the responsible agencies for making the management decisions for audit findings that relate to federal awards made to subrecipients. If the state is going to adopt a requirement for OMB A-133 requirements, it must be consistent with OMB A-133 and responsibility for management decisions is a task assigned to counties.

"OMB A-133 contains a definition of a recipient in subsection .105 which is consistent with the definition of recipient in the Federal Single Audit Act (31 U. S. C. § 7501 (a)(1 7)). A "recipient" is a nonfederal entity that expends federal awards received directly from a federal awarding agency to carry out a federal program - the State of California.

"Under OMB A-133, section .105, the "pass-through entity" means a nonfederal entity that provides a federal award to a subrecipient to carry out a federal program. In the hierarchy of OMB A-133 decisions, as well as the definitions in the Federal Single Audit Act, management decisions in California are the responsibilities of the counties.

"Although the Department of Social Services establishes the AFDC-FC payment *rate* for group homes and foster family agency programs, the group homes and foster family agencies do not receive any AFDC-FC *payments* directly from the Department. Individual foster children are placed in a group home, foster family agency, or other type of foster care facility, by county social services and probation departments. The county placing agency and provider enter into a placement agreement for each child, which specifies their mutual responsibilities, including the rate that will be paid to the provider by the county.

"When a child is placed in foster care, the county social worker or probation officer responsible for his/her case applies for assistance under the AFDC-FC program. If an eligibility worker in the county social services department (in a unit that is administratively separate from the social workers) determines that a child meets all of the eligibility requirements for the AFDC-FC program, then the county is able to obtain 40% financial participation from the state for the costs of the payments made to the foster care provider. If the child is determined to meet the eligibility requirements for the federal Title IV-E AFDC-FC program, then federal financial participation is available for approximately half of payments

made for activities that fall under the Title IV-E definition of "allowable," with the state and county sharing the non-federal share of costs at a 40% state/60% county ratio.

"Counties are able to claim financial participation through the AFDC-FC program only for payments made to providers who have a state-established AFDC-FC payment rate and meet the definition of "eligible facility" (e.g., group homes and foster family agencies operated on a nonprofit basis and licensed to do business in California as "community care" facilities). Therefore, group homes and foster family agencies interested in having foster children placed in their facilities by the counties apply on an annual basis to obtain such a rate from the Department of Social Services Foster Care Rates Bureau (FCRB). Further, since counties cannot claim financial participation through the AFDC-FC program for the portion of any payment that exceeds the state-established AFDC-FC rate for a facility, most group homes and foster family agencies agree to accept, as fall payment for providing care and supervision to a foster child, an amount equal to the AFDC-FC rate established for their facility by the FCRB. However, in more and more cases, providers request, as a condition for accepting foster care placements, an amount higher that the AFDC-FC rate established by FCRB because the AFDC-FC rates have fallen significantly behind increases in the cost of doing business over the past two decades. In fact, at least one county (Santa Clara) pays all of the group homes in its county rates that are higher than the state-established AFDC-FC rates, in recognition of the fact that the latter are inadequate to cover the reasonable costs of operating a group home facility in a high-cost area such as Santa Clara County.

"While group homes and foster family agencies are required to have a license issued by the Department of Social Services Community Care Licensing (CCL) Division in order to operate, and may have received an AFDC-FC payment rate from the Department FCRB, there is no contractual relationship between group homes and foster family agencies and the Department. The issuance of a CCL license and an AFDC-FC rate does not create mutual obligations between the Department and the provider with regard to foster care placements and/or AFDC-FC payments. Indeed, the Department cannot refer foster children for placement because that is the responsibility of county social services and probation departments. Similarly, the Department has no obligation to make AFDC-FC payments to group homes and foster family agencies.

"For the purposes of foster care placements and AFDC-FC payments (as opposed to AFDC-FC rate-setting), group homes, foster family agencies, and other foster care providers have a contractual relationship through their placement agreements with the counties; not with the state. For the purposes of claiming reimbursement under the AFDC-FC program for the costs of foster care placements, the counties have a relationship with the state.

"This regulation violates both the consistency and authority provisions of the Administrative Procedure Act by adopting a management decision process which is inconsistent with both the Federal Single Audit Act (31 U.S.C. § 7501) and the federal government's implementing definitions contained in OMB A-133." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. The Department has recently received additional clarification of the audit requirements from the federal DHHS. The DHHS has confirmed that California foster care group home and FFA providers are sub-recipients and therefore, subject to OMB Circular A-133 audit requirements. As a result of the DHHS clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulation package.

While the definition of "pass-through" entities in OMB Circular A-133 may include counties, the "State established *rate system*" in California does not provide for a mutually exclusive relationship between the pass-through counties and their sub-recipients. Many of the sub-recipients receive placements and payments from more than one county at any given time making the counties' ability to act as the single pass-through entity for the audit and management decisions administratively cumbersome. Therefore, in order to simplify the process and to provide consistency, the Department will serve as the pass-through entity for purposes of the audit and management decisions. The Department will issue a re-notice and make the revised regulation package available for comment.

Section 11-400r.(3)

21. Comment:

"This section adds foster family agencies to the involuntary collection procedure for recovering a sustained overpayment of a self-reported overpayment that applies to a group home provider.

"Welfare and Institutions Code sections 11466.22 and 11466.3 1, by their own explicit definitions, apply only to group homes; they do not apply to foster family agencies. It is clear because Welfare and Institutions Code section 11466.22(b) refers to group homes as defined in subdivision (h) of section 11400. That definition states:

"'Group home' means a nondetention privately operated residential home, organized and operated on a nonprofit basis only, of any capacity, that provides services in a group setting to children in needed care and supervision, as required by paragraph (1) of subdivision (a) of Section 1502 of the Health and Safety Code.

"A foster family agency is a nonprofit organization that recruits foster parents to provide services to children in their homes. A foster family agency, as such, is not and does not, directly provide residential home services at all. Rather, it recruits and qualifies individuals to provide those services. Further, the services are not provided in a group setting; rather, in the separate homes of the foster families.

"Finally, this involuntary collection procedure has no potential application to disallowed cost recoupment compliance in accordance with OMB Circular A-133. A review of OMB Circular A-133 has no reference to an involuntary collection procedure.

"The Initial Statement of Reasons indicates the purpose of this regulation is to amend for clarity and consistency with Welfare and Institutions Code sections 11466.22 and 11466.31 and to ensure compliance with OMB Circular A-133 disallowed cost recoupment requirements. The proposed regulation violates the authority, consistency and necessity standards of the Administrative Procedure Act." (Alliance)

Response:

The Department thanks the testifier for their comments. Existing regulations at MPP Section 11-403(j) refer the reader to group home overpayment regulations for FFAs. The addition of FFAs to this section is for clarification purposes only and does not represent a change in policy. Clarification is necessary to ensure that costs disallowed as a result of an A-133 audit can be recovered from FFAs and group homes. Specifically, because A-133 requires recovery, the Department will identify misuse and fraud and recoup the disallowed costs from FFAs and group homes. The Department will issue a re-notice and make the revised regulation package available for comment.

Section 11-400r.(4)

22. Comment:

"This section adds a new definition of an RCL reduction resulting from program change applications, a provisional rate program audit or a nonprovisional program audit. It is not necessary to implement OMB A-133 audits and thus fails the statutory requirement of "necessity." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department is providing an accurate definition of RCL reduction for consistency with existing policies. The existing RCL Reduction definition was incorrect and correctly applied to the term Rate Payment Offset. Therefore, a definition for RCL reduction was developed, rather than deleting it. Lastly, the Department is not limited in the scope of this package to items related to A-133. Concerning comments on the Department's authority to implement regulations, the Department has authority under Welfare and Institution Code Sections 10553(e) and 10554 to formulate and adopt regulations. Welfare and Institutions Code Section 11460 designates the Department as the single organizational unit whose duty is to administer a state program for establishing foster care rates. Welfare and Institutions Code Section 11461.5 authorizes the Department to develop regulations concerning group home rates. Welfare and Institutions Code Section 11463 authorizes the Department to develop a rate system for FFAs and to develop regulations concerning FFAs. The Department will issue a re-notice and make the revised regulation package available for comment.

Sections 11-402.6, 11-402.63, 11-402.636, and 11-402.636(a)

23. Comment:

"These sections provide that the Department, through a "management decision," can recoup expended AFDC-FC program funds on unallowable costs. This violates the Administrative Procedure Act rules for consistency, authority and necessity.

"Welfare and Institutions Code section 11462, subdivision (f) still unequivocally provides for a standardized schedule of rates based upon a rate classification level between I and 14, with the associated points. It still provides for a fixed monthly rate per child to provide the applicable level of services. Group homes must provide for children's needs and they are paid the standardized rate to meet those needs. For example, children may require dental work, yet dental costs are not allowable federal costs. Children may require medical care, yet medical costs are not allowable under Title IV-E. Many of the children in group homes, particularly the higher level group homes, have identified mental health diagnoses and they must have the treatment of psychiatrists who prescribe and monitor their medication needs and provide counseling services, including mental health counseling services by psychiatrists. These are not allowable federal costs.

"Social work activities are not allowable federal costs; however, they are allowable under California state law. Historically, the state has simply made a policy decision to pay for social work activities so the children receive social work services in addition to paying for their care and supervision. While social work activities are not allowable federal costs, they are an allowable state cost.

Group homes have been, and continue to be, required to report costs to the State of California and these reports are used for the state to claim federally-allowable costs. The state has not attempted to collect overpayments based on federally-allowable costs. Further, the recoupment of unallowable costs is not an OMB A-133 implementation issue. Which is to say, there is no federal mandate that the state must recoup federally-unallowable costs from providers. Certainly, the allowability of federal costs reported by providers to the state influences, and will continue to influence, the amount of money the state can claim for reimbursement from the federal government. But a financial audit implementation mandate, assuming that the federal government ultimately determines that OMB A-133 audits are required, does not change the state/federal claiming responsibility and does not contain an implied mandate for the state to recoup unallowable costs from the provider community. The Initial Statement of Reasons indicates that this section is necessary to ensure that California meets the federal audit standard for the foster care program as required under OMB Circular A-133 for purposes of overpayment recovery and that Title IV-E federal financial participation in the program is not jeopardized.

"OMB A-133 section .405 details the requirements for management decisions. Setting aside the fact that it is a county responsibility and not a state responsibility, assuming that a particular audit finding identified that unallowable costs were expended (for example, to purchase social work or medical services), the auditee may or may not be required or expected to repay the disallowed costs. Clearly, under current California law, the auditee should not be required to repay either disallowed social work costs or medical costs. On the other hand, the disallowed costs do limit the state's federal claims. Yet, the regulation appears to mandate repayment of all disallowed or unallowable costs.

"The capitated rate system, contained in Welfare and Institutions Code section 11462, mandates payment of a fixed monthly rate. It is inconsistent with that statute to superimpose provider cost reimbursement to the State of California based on OMB A-133 or OMB A-122 principles. All of the cost reimbursement principles in OMB A-122 are explicit - they apply only to a cost reimbursement system. In fact, OMB Circular A-122 in paragraph 3, at pages 21, 22 and 23, makes clear that the cost principles do not apply to federal awards under which an organization is not required to account to the federal government for actual costs incurred. A copy of OMB A- 122 is attached hereto as Exhibit "8." The capitated system, or flat-rate system, in Welfare and Institutions Code section 11462 is a system in which the nonprofit agency is not required to account to the federal government for actual costs incurred. In fact, they are not even considered in the rate setting function; rather, rates are set on the basis of the number of points projected which match the level of services associated with the points. Under California's rate setting system, an individual provider at RCL 10 receives a fixed amount of money regardless of whether its costs are in excess of that amount or less than that amount.

"The California Alliance acknowledges that if the federal government finally determines that OMB A-133 audits are required, the state may implement that decision through a change in the statute but not through a regulatory change. Before either OMB A-133 principles or OMB A-122 cost principles apply, the system needs to be converted to a cost reimbursement system. To change that, the California statutory law must change. These regulations violate the statutory mandates for authority, consistency and necessity for the reasons discussed above." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. The testifier is incorrect that as the result of the A-133 audit, the Department cannot recoup any identified unallowable costs through a management decision. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has confirmed that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients, and therefore subject to OMB Circular A-133 audit requirements. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received.

With respect to the testifier's concerns regarding the Department's authority to collect overpayments, the legislature has in Welfare and Institutions Code Section 11466.2 and 11466.21 authorized the Department to conduct or have conducted fiscal and financial audits. Implicit in this authority is the power to require remediation of findings made in those audits. Moreover, OMB Circular A-133 requires among other actions, recovery of unallowable costs. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. The Department will issue a re-notice and make the revised regulation package available for comment.

Sections 11-402.66, 11-402.664, and 11-402.665

24. Comment:

"These provisions implement the unallowable cost recoupment provisions and, for all of the reasons expressed above, the California Alliance objects to them as violating the statutory criteria for authority, consistency and necessity." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. With respect to the Department's authority to recoup overpayments, the legislature has in Welfare and Institutions Code Sections 11466.2 and 11466.21 authorized the Department to conduct or have conducted fiscal and financial audits. Implicit in this authority is the power to require remediation of findings made in those audits. Moreover, OMB Circular A-133 requires among other actions, recovery of unallowable costs. The Department will issue a re-notice and make the revised regulation package available for comment.

Sections 11-402.8 and 11-402.82

25. Comment:

"These provisions change an existing regulation which contains a cost reporting mandate and completely change it to eligibility for AFDC-FC reimbursement. The existing regulations require group homes to report costs in accordance with applicable provisions of the federal regulations. In fact, existing section 11 -402.8 is captioned "Cost Reporting." The California Alliance has understood for the last 11 years that all providers have an obligation to report costs in accordance with the federal regulatory requirements so that the State of California can claim allowable reimbursement from the federal government. It is an unwarranted change to the rate setting system to prohibit payment for unallowable federal costs such as dental care, medical care, psychiatric care, medication monitoring, etc. All of those activities must be provided to children in care in order to meet their individual needs. This section, however, substantially changes the rate setting system from the previously discussed flat rate or capitated system to a system that only allows expenditure for federally-allowable costs.

"The last phrase, "In addition to other costs listed in MPP section 11-402.8" is ambiguous. Attached hereto as Exhibit "9" and incorporated herein by this reference is a current copy of the MPP section 11-402.8 series. These sections make clear that the capitated rate system pays providers for both federally-allowable and federally-unallowable costs. The ambiguity is caused by the limitation to actual, allowable and reasonable costs as "defined in federal

statute and regulations" in addition to other costs listed in MPP sections 11-402.8. There are both federally-allowable and federally-unallowable costs listed in section 11-402.8.

"Actually, there are a number of differences in the 11-402.8 series with the OMB A-122 cost reimbursement principles and the compliance testing principles in OMB A-133. For example, section 11-402.822 allows social work activities. That is not an allowed cost under the federal rules. Section 11-402.823 allows actual principal and interest on original acquisition mortgages. The federal rules are different under OMB A-122. While depreciation and use allowances are allowed under OMB A-122, it excludes the cost of land. Acquisition costs, as such, are excluded. The interest on original acquisition mortgages, which is allowed under section 11-402.823, appears to be excluded under OMB A-122 (section 23(a)).

"Section 11-402.824 allows reasonable lease or rental costs on real property. OMB A- 122 in paragraph 46 has different limitations on rental costs than the 12% of fair market value limitation in section 11-402.828(a)(1).

"Another significant difference between the Department's rate regulations and the section 11-402.8 series and the OMB A-122 principles concerns overhead or administrative costs. Essentially, there are not limitations for allowable activities under the state system but there are mandated allocation requirements in OMB A-122.

"The above differences are intended to be examples of the inconsistencies which the proposed regulations will necessarily cause because of the simultaneous reference to federal cost reimbursement systems (OMB A-133 and OMB A-122) and the retention of the capitated rate system. Not only will the rules be different causing substantial ambiguity or lack of clarity, but it also means that the total rate which is statutorily mandated will be reduced. The above regulation violates the statutory criteria for authority, consistency, clarity and necessity." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Specifically, the DHHS has confirmed that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients, and therefore subject to OMB Circular A-133 audit requirements. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in

which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in which they were received.

With respect to the testifier's concerns regarding the Department's authority to collect overpayments, the legislature has in Welfare and Institutions Code Section 11466.2 and 11466.21 authorized the Department to conduct or have conducted fiscal and financial audits. Implicit in this authority is the power to require remediation of findings made in those audits. Moreover, OMB Circular A-133 requires among other actions, recovery of unallowable costs. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. The Department will issue a re-notice and make the revised regulation package available for comment.

Section 11-402.82

26. Comment:

"Item six

"In a separate arena, the concept of "the determination of reimbursable costs for group home programs" was mentioned in Section 11-402.82. This concept of reimbursable costs must be clearly constrained so that reimbursements do not exceed rates. Prior to the establishment of the current rate setting system, several larger group home providers were able to provide allowable reimbursable costs through private donations and United Way contributions. When the current rate system was enacted, if previous allowable reimbursable costs exceeded propose rates, the higher amount was paid to assure a continuity of care." (TTP)

Response:

The Department thanks the testifier for their comments. However, it is unclear what concern the testifier is raising. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients, and therefore subject to OMB Circular A-133 audit requirements. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used to serve or benefit foster care children, regardless of the fiscal year in

which they were received. The Department will issue a re-notice and make the revised regulation package available for comment.

27. Comment:

"Item seven

"House keeping: Section 11-402.82 mentions regulations 45 CFR 1356. I was unable to fide any definition of the acronym CFR in FRC 11-400 or the Authority and References Citations." (TTP)

Response:

The Department thanks the testifier for their comments. "CFR" is the acronym for the "Code of Federal Regulations."

Section 11-403(c)

28. Comment:

"The existing rate regulations in the section 11-403 series deal with foster family agencies. Subdivision (c) of section 11-403 is proposed to be changed so that foster family agencies are ineligible for Title IV-E reimbursement unless all costs are actual, allowable and reasonable as defined in federal statutes and regulations including MPP section 11-402.8 and 11-405. All of the same problems regarding eligibility for Title IV-E funding for group homes are imported into the capitated foster family agency reimbursement system.

"The foster family agency reimbursement system is not contained in statute, but in the section 11 -403 rate regulations. A copy of those regulations is attached hereto as Exhibit "10" and incorporated herein by this reference.

"Basically, the foster family agency receives a foster family agency basic monthly rate, depending upon the age of the children, plus an increment for the child and an increment for social work activities. Whatever the dollar value, it is a flat monthly rate and is unrelated to the expenditures incurred by the foster family agency for the provision of foster parenting services for children. Again, the proposed regulations change the capitated rate to a system which limits expenditures to actual, allowable and reasonable as defined in federal regulations and in MPP section 11-402.8. That is a fundamental change in the rate setting system and should not be made under the guise of implementation of an OMB A-133 audit requirement. The proposed regulations violate the necessity, consistency, authority and clarity requirements." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulations. Specifically, the Department has deleted "eligible" and is only seeking actual allowable and reasonable costs to be reported. These cost reporting requirements are being made consistent with the requirement for non-profit corporations operating a group home. The Department will issue a re-notice and make the revised regulation package available for comment.

Section 11-403(j)

29. Comment:

"The Initial Statement of Reasons indicates this amendment is necessary for accuracy in the regulations to eliminate reference to obsolete regulatory citations. Although it has little relevance to implementation of OMB A-133 audits, the change is significant.

"Under the existing regulatory reference in section 11-402.8, is a reference to "Cost Reporting." Under the system that has been in place for the last 11 years, foster family agencies must report costs for federal claiming purposes and the costs must be reported in a manner consistent with federal cost claiming rules.

"The changed reference to section 11-402.6 deals with the payment of overpayments, not federal cost reporting. The reference to section 11-402.6 deals with overpayments resulting from a group home provider self-reporting an overpayment on a program or fiscal audit. There is no "program audit" for a foster family agency, as there is no point count system. Yet, apparently the Department is going to change the audit procedure for foster family agencies and attempt to implement some currently nonexistent program audit procedures. Not only does this have nothing to do with implementing OMB A-133 audits and thus violates the necessity criterion, but it will also create significant ambiguity in the regulations because there are no program audits for foster family agencies. To subject a foster family agency to the program audit overpayment regulations when there is no point-based level of care system violates the statutory mandates for authority, consistency and necessity.

"The Department's Initial Statement of Reasons misstates the effect of this change. It does not merely correct a reference citation as an obsolete citation. The existing reference to section 11-402.8 made clear that cost reporting principles

contained in those sections apply to foster family agencies and this arguably technical cleanup converts it to a cost reimbursement system with provision for overpayment of unallowable costs." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. The Department is correcting an inappropriate regulation citation that did not apply to overpayments, which is the subject matter for this section. The existing citation references the cost reporting section and instead, should have referenced overpayments, which was the original intent. The Department will issue a re-notice and make the revised regulation package available for comment.

Sections 11-405.1, 11-405.11, 11-405.112, 11-405.13, and 11-405.136

30. Comment:

"There are two primary problems with these sections. First, section 11-405.11 again confuses "fiscal audits" and "financial audits" by defining fiscal audits as audits performed both by the Department and/or certified public accountants, etc. Under the applicable Welfare and Institutions Code statute in section 11466.21, it is clear that certified public accountants or state-licensed public accountants prepare financial audits and the state does not perform financial audits. Conversely, there is no statutory authority for certified public accountants to prepare or conduct "fiscal" audits. The California Alliance acknowledges that if a certified public accounting firm were retained by the state as the state's agent or designee, a certified public accounting firm could perform a fiscal audit. If that is the relationship intended, then the sections should be clarified. In short, this provision is inconsistent with the statutory authorizing legislation in Welfare and Institutions Code section 11466.21.

"The more significant problem is contained in section 11-405.13. This allows "fiscal audits" to be performed according to the cost reimbursement-based rules in OMB Circular A-122. This is the Circular that is predicated on the existence of a cost reimbursement system and as we have demonstrated previously, the current statutory rate system is not a cost reimbursement system. The practical impact of mandating fiscal audits according to federal cost reimbursement standards is that the provision of social work will be an unallowable federal cost, yet mandated in the California statutes; the provision of medical care to children will be an unallowable federal cost; the provision of dental care to children will be an unallowable federal cost; and the provision of psychiatric services to monitor and maintain medications for children will be an unallowable federal cost. Other provisions of the regulations which we have previously discussed, declare both a

group home and a foster family agency ineligible to receive Title IV-E funds if they spend or expend unallowable federal costs.

"Because for the last 11 years the cost provisions in the rate regulations in section 11-402.8 have been cost reporting requirements, the conversion in these regulations as a precondition to eligibility to receive Title IV-E funds and to mandate the recovery of overpayments will be inconsistent with the authorizing legislation, prevent needed medical, dental and psychiatric treatment for children in care, and is not necessary to the implementation of an OMB A-133 audit requirement. These regulations violate the statutory Administrative Procedure Act requirements of authority, consistency, clarity and necessity." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Welfare and Institutions Code Section 11466.2 provides statutory authority for the Department to have a CPA conduct a fiscal audit. Since release of the regulation package, the Department has received additional clarification of the audit requirements from DHHS. Specifically, the DHHS has determined that OMB Circular A-122 Cost Principles do not apply to California's capitated rate system and confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients, and therefore subject to OMB Circular A-133 audit requirements. As a result of this clarification, input from the provider community, and testimony receive the proposed regulations, the Department has made revisions to the regulations. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. Furthermore, the Department identified a broad range of activities in which unexpended funds may be used for activities that serve or benefit foster care children, regardless of the fiscal year in which they were received. Further, regarding the reference to Section 11-402.8, the Department has deleted the precondition to eligibility for AFDC-FC reimbursement and retains existing regulatory language. The Department will issue a re-notice and make the revised regulation package available for comment.

Sections 11-405.2, 11-405.21 and 11-405.213

31. Comment:

"Section 11-405.213(b) changes the discretionary utilization of OMB Circular A-133 audits to the mandatory use of OMB Circular A-133 audits for corporations who expend $300,000 or more for their programs and activities. For the reasons argued previously regarding the preliminary nature of the Region IX

vendor/subrecipient status determination, these regulations are not necessary and are premature." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, the Department has received additional clarification of the audit requirements from the federal DHHS including confirmation that group home and FFA providers are subrecipients subject to OMB Circular A-133 audit requirements.

In order to protect and preserve California's eligibility for federal financial participation under Title IV-E, the Department has determined that regulations implementing OMB Circular A-133 are necessary. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulation package. The Department will issue a re-notice and make the revised regulation package available for comment.

Section 11-405.215

32. Comment:

"This provision requires compliance testing pursuant to OMB Circular A-133. Again, for the reasons previously discussed, it is premature and thus violates the Administrative Procedure Act necessity criterion." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, the Department has received additional clarification of the audit requirements from the federal DHHS including confirmation that group home and FFA providers are subrecipients subject to OMB Circular A-133 audit requirements. As a result of this clarification, input from the provider community, and testimony received on the proposed regulations, the Department has made revisions to the regulation package including deletion of this section since specific reference to compliance testing is already specified in OMB Circular A-133. The Department will issue a re-notice and make the revised regulation package available for comment.

Section 11-405.217

33. Comment:

"This regulation requires information to be reported in accordance with standards established by the Financial Accounting Standards Board, GAGAS (Generally Accepted Government Auditing Standards) standards, and OMB A-133 standards. Since each of those standards may be different, this regulation may cause substantial ambiguity. Additionally, the OMB A-133 standards are premature for the reasons previously discussed." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. As any industry requires, the need for guidance via standards, is desirable to ensure consistency in application and comparability among reporting entities. Financial accounting standards dictate the guidelines for ensuring consistency and comparability of accounting information that is presented in an audit report. However, auditing standards provide consistency and comparability in placing reliance on the fairness of reported financial statements. Both are necessary to provide reliability and relevance to a non-profit corporation's financial results of operations. Those employed in the accounting and auditing industry comprehend and rely on this necessary framework. Foster care providers require the services of both accountants and/or auditors in order to comply with the audit requirements, whether employed by the provider or providing consulting services. As a courtesy to their clients, and when requested, accountants and auditors explain these standards and the application of them in their services to foster care providers. Accounting and auditing standards, as explained previously, work in concert.

We respectfully disagree with the testifier's claim that OMB Circular A-133 standards are premature. The Department received additional clarification from DHHS in February 2002 that reiterated the requirement for the OMB A-133 standards. In order to protect and preserve California's eligibility for federal financial participation under Title IV-E, the Department has determined that regulations implementing OMB Circular A-133 are necessary. The Department will reissue a re-notice and make the revised regulation package available for comment.

Section 11-405.219

34. Comment:

"The subject matter of this section is rate termination and it is unrelated to implementation of an OMB A-133 audit requirement and thus fails the necessity criterion." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. However, the general section, 11-405 concerns the audit and the necessary audit requirements to ensure that the report is acceptable. The consequence to fulfill the audit requirement is the subject matter of the Section 11-405.219. As provided in Welfare and Institutions Code Section 11466.21, in order to receive a rate, a provider must submit an acceptable audit report. The failure to submit an audit as required by statute is rate termination and correctly reflected in 11-405.219. The Department will reissue a re-notice and make the revised regulation package available for comment.

Sections 11-405.24 and 11-405.241 through 11-405.249

35. Comment:

"This regulation implements management decisions on audit findings resulting in disallowed costs. Specifically, they provide an appeal right. While the California Alliance does not object to an appeal right, the California Alliance objects to the implementation of the management decision for all of the reasons previously identified. Management decisions are, under OMB A-133, county functions or responsibilities of the "pass-through entity." Thus, any appeal process should be a county process. Additionally, it is not necessary to implement a management decision process because it is premature to even implement the OMB A-133 audit process. The provisions of this proposed regulation, therefore, violate the statutory criteria for authority, consistency, necessity and clarity.

"Section 11-405.243 establishes an evidentiary standard that mandates the group home to make documents available by the date the group home or foster family agency requests a hearing. Generally, under most administrative procedures, if there is to be a hearing by an impartial hearing officer, and that requirement is generally mandated by due process, the parties may introduce evidence at the hearing. This section impermissibly limits the right of group homes and foster family agencies to introduce evidence at the hearing and thus denies them a fair hearing in violation of their state and federal due process rights.

"Subdivision 11-405.247 also indicates the hearing is to be conducted in accordance with the existing procedures in sections 11-430.5 through 11-430.69. Section 11-430.662 allows and gives the parties a "right" to introduce documents or exhibits. Hence, the effort to limit the provider's right to introduce documents creates an ambiguity because the two sections are internally inconsistent. This provision violates the necessity and clarity standards.

"That concludes the comments of the California Alliance. We urge the Office of Administrative Law to reject this regulatory package for the reasons indicated." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into development of the OMB Circular A-133 regulations. Since release of the regulation package, the Department has received additional clarification of the audit requirements from the federal DHHS. The DHHS has confirmed that California foster care group home and FFA providers are considered to be sub-recipients and therefore, subject to OMB Circular A-133 audit requirements.

While the definition of "pass-through" entities in OMB Circular A-133 may include counties, the "State established *rate system*" in California does not provide for a mutually exclusive relationship between the pass-through counties and their sub-recipients. Many of the sub-recipients receive placements and payments from more than one county at any given time making the counties' ability to act as the single pass-through entity for the audit and management decisions administratively cumbersome. Therefore, in order to simplify the process and to provide consistency, the Department will serve as the pass-through entity for purposes of the audit and management decisions.

Section 22-405.243 mirrors the evidentiary standard applicable to appeals of the Department's provisional rate RCL determinations that is prescribed by Welfare and Institutions Code Section 11462(c). The evidentiary restriction to limit documentary evidence that is presentable at hearing to those documents made available in the request for appeal is necessary to ensure efficient administration of the Department's financial audit responsibilities and to avoid the fraudulent creation of records. Because a non-profit corporation may introduce documents or exhibits at the hearing that have been made available in its request for hearing, there is no inconsistency with a party's right to introduce documents and exhibits as provided in MPP Section 11-430.662. The Department will reissue a re-notice and make the revised regulation package available for comment.

g) 15-Day Renotice Statement

Pursuant to Government Code Section 11346.8, a 15-day renotice and complete text of modifications made to the regulations were made available to the public following the public hearing. The following written testimony was received from the California Alliance of Child and Family Services (Alliance) and Los Angeles County Department of Children and Family Services (Los Angeles) as a result of the 15-day renotice.

OBJECTIONS BASED ON NECESSITY, AUTHORITY AND CONSISTENCY

1. Comment:

"The Alliance commented by letter dated January 16, 2002, and began its comments with a general objection based on necessity, authority and consistency. Concerning issues related to the implementation of OMB A-133 audits, the Alliance now acknowledges that the federal determination appears final. That determination related to the "vendor" "subrecipient" distinction; however, the Alliance still believes that under the necessity criteria this regulatory package should be limited to the implementation of OMB A-133 audits. That would be directly responsive to the Department of Health and Human Services' decision regarding subrecipient status, which requires an OMB A-133 audit if the $300,000 threshold is exceeded. To the extent that the proposed regulations go beyond issues associated with the implementation of OMB A-133 audits, we submit the regulatory package violates the necessity criteria in the Administrative Procedure Act." (Alliance)

Response:

The Department thanks the testifier for their comments and appreciates their time and effort devoted to providing input into the development of these regulations. The Department has the authority to include other amendments as deemed necessary to provide clarity and consistency for the operational application of regulations.

2. Comment:

"The Alliance also objected to various provisions in the package with regard to authority and consistency. The primary continuing objection based on these regulatory criteria is that the recoupment provisions of fiscal audits, fraud and/or misuse audits, and potentially OMB A-133 audits, fundamentally change the nature of the rate setting system from a capitated system to a rate maximum system. We developed those arguments extensively in our January 16, 2002 comments. We note one significant change as a result of this regulatory package. This regulatory package

reinstitutes the historical rule that expenditures on non-federally allowable costs are a cost reporting issue, not a recoupment issue. Nevertheless, the state does intend to recoup monies based upon fiscal audits and fraud and/or misuse audits. That fundamentally changes the nature of the capitated rate system. As we previously discussed, if a provider is to receive an RCL 10 at, for example, $4,858 per month, per child, so long as the provider provides the services associated with that rate classification, there should not be recoupment of monies which lower the provider's effective rate. Without changes in the statutory provisions regarding the setting of rates (Welf. & Inst. Code §§ 11462, 11462.01) which determine the rate classification level and the associated payment levels, recoupment of program funds violates the statutory provision for a capitated rate. In other words, if the Legislature wants to change the capitated or flat rate system it may do so, but the Department may not change the capitated rates in this regulatory package." (Alliance)

Response:

The Department thanks the testifier for their comments. Since the release of the 45-day notice, the Department has received additional clarification of the audit requirements from the Department of Health and Human Services (DHHS). Specifically, DHHS has confirmed that non-profit corporations who operate a group home and/or foster family agency are deemed subrecipients, and therefore subject to OMB Circular A-133 audit requirements. Additionally, based on Welfare and Institutions Code Section 11460 and the Department's role in ensuring that AFDC-FC funds are expended on purposes for which they were intended, the use of state and federal AFDC-FC program funds regulations were developed. In addition, the Legislature recognized the applicability of allowable cost principals to group homes in Welfare and Institutions Code Section 11462.06, by making the reasonable costs of leases for shelter care for foster children an allowable cost.

3. Comment:

"To the extent that the regulatory package seeks to go beyond OMB A-133 audit implementation issues, this regulatory package, as re-noticed in the 15-day period, is not "sufficiently related" for purposes of Government Code section 11346.8(c)." (Alliance)

Response:

The Department thanks the testifier for their comments and appreciates their time and effort devoted to providing input into the development of these regulations. The Department has the authority to include other amendments as deemed necessary to provide clarity and consistency for the operational application of regulations.

4. Comment:

"The remaining comment will include references to different types of audits that are included in the regulatory package. References to a "financial audit" will relate to the annual audit performed by a certified public accountant. References to a "fiscal audit" or a "fraud and/or misuse audit" will refer to audits performed by the State of California or the federal government. References to a "program audit" refer to audits to determine compliance with the level of services associated with a paid rate classification level.

"With regard to financial audits fiscal audits and fraud and/or misuse audits, the Alliance submits the regulatory package remains ambiguous, duplicative and is unclear. The best way to demonstrate the concerns or lack of clarity regarding the audits, their associated recoupment procedures and administrative review procedures, is to ask the following questions:

"1. Is a fiscal audit a separate audit from a fraud and/or misuse audit or are they the same? For example, is a finding of fraud and/or misuse a finding that would result from either a fiscal audit, a financial audit or even a program audit? Or does the Department intend, through these regulations, to create a separate category of audit which will focus specifically on the identification of issues regarding fraud and/or misuse?

"2. Why did the Department apply the management decision process to fiscal and/or fraud or misuse audits? Section 11-405.231 addresses the "Administrative Procedures for Recoupment." In subdivision .231(a), the proposed regulations apply the procedures to a financial audit. The Alliance believes that the use of the management decision process should properly apply to the review of certified public accountant-performed financial audits. However, subdivisions .231(b) and .231(c) also apply the management decision process to fiscal audits and fraud and/or misuse audits. The management decision review process for fiscal and fraud and/or misuse audits appears to duplicate the administrative review procedure already in the Department's rate regulations (MPP § 11-430, et seq.). Does the Department intent to have alternative review procedures and, if so, when will the management decision process be employed and when will the existing review procedures be employed?

"3. In the management decision review process following a financial audit, what standards or rules will the Department use with regard to audit findings or audit exceptions contained in the certified public accountant's financial audit? If a certified public accountant's financial audit finds that the financial statements fairly represent the financial position of the non-profit corporation, does the Department intend to disagree with that conclusion? If so, what standards or rules will the Department apply in disagreeing? If the certified public accountant audit finds that there are adequate internal controls or makes a recommendation to enhance internal controls, what standards or rules does the Department intend to employ in reviewing that finding? If a certified public accountant financial audit does not contain an audit exception, does the Department intend to create audit exceptions during the review process? If so, again, what standards or rules will the Department apply in reviewing the certified public accountant-performed audit?

"The Alliance respectfully requests the Department respond to the questions in its response to these comments, as the Department's response will assist the Alliance members in knowing how this regulatory package will be applied." (Alliance)

Response:

The Department thanks the testifier for their comments. In response to question 1 pertaining to fiscal audits, there is no intent to create a separate category of audit. A fiscal audit is an audit conducted to determine whether financial information submitted by a group home or foster family agency is accurate and supported and to determine whether misuse or fraud has occurred. A fiscal audit's objectives relate to the budgetary and financial aspects of an organization, and the scope of a fiscal audit could vary from limited to complex depending on the specific review objective. A fiscal audit may include or result in an investigative review of a corporation when there is sufficient information provided that misuse of funds or fraud may have occurred. A fiscal audit may be initiated following concerns expressed regarding possible misuse or fraud identified in the Department's review of a group home or foster family agency's financial audit report; from information provided by Foster Care Program Audit, Community Care Licensing or other Department staff; or even through an anonymous phone call or letter. A finding of misuse and/or fraud may result from a fiscal audit or a financial audit.

In response to question 2 regarding the application of the management decision process to fiscal audits, the Department intends to use a consistent process for evaluating financial information from financial audits and fiscal audits and issuing management decisions on audit findings, including any action expected of the corporation. For a financial audit report, the Department will issue a management decision within six months of receipt of

the report. The Department may issue a management decision upon completion of a fiscal audit if deemed necessary and appropriate. Any management decision which addresses recoupment of funds from the provider will be based on a review of the audit findings, any responses from a non-profit corporation to the findings, and findings from any additional audits conducted by the Department or its designee. The administrative review procedures as set forth in MPP Sections 11-403.5 through 11-403.69 will be employed within 60 days of the request for a hearing on the management decision.

In response to question 3 regarding the management decision process following a financial audit, the Department will follow the review process as described in OMB Circular A-133 Subsection .405. With respect to accepting or disagreeing with information presented by the certified public accountant in a financial audit report, the Department reserves the right to contest any reported information if there is evidence to dispute the information. The Department's oversight responsibilities would not be met if there is blind acceptance of all reported information. The rules to be applied are those that govern issues of accountability and financial reporting. For example, if food expenses of $15,000 are reported, it is expected that the provider can submit adequate documentation to substantiate such expenses, such as food receipts. A non-profit corporation will have the opportunity to respond to the audit findings presented in a management decision.

Section 11-400f.(7)

5. Comment:

"The proposed revisions strike the reference "by the Department." This section should be made consistent with section 11-405.11, which specifies that fiscal audits may be performed by the Department, its agents, or an audit agency of the federal government. Welfare and Institutions Code section 11466.2 is the applicable statutory provision, which authorizes performance of fiscal audits. That section requires the Department "perform, or have performed" group home program and fiscal audits. We note further that the applicable federal law requires that the "state shall arrange for a periodic and independently conducted audit of the programs assisted under this part…" (42 U.S.C. § 671(a)(13).)

"In order to be consistent with section 11-405.11, the state implementing law and the federal law, either the Department should reinsert the phrase "by the Department" or employ the same language employed in section 11-405.11. We will later recommend that the language in section 11-405.11 be changed to strike the reference to "agent" and substitute the term "designee," which appears to be more consistent with the authorizing federal and state statutes.

"This definition also contains a reference to misuse or fraud. Both fraud and misuse are then separately defined in section 11-400f.(13) and section 11-400m.(5). The statutory provisions regarding fiscal audits are contained in Welfare and Institutions Code section 11466.2 (for group homes) and Welfare and Institutions Code section 11463.5 (for foster family agencies). Because there is no statutory definition of a "fiscal audit" in the Welfare and Institutions Code, presumably, the Department is adopting a regulatory definition. We have several observations. First, fraud and/or misuse audits are separate from financial audits, which are the types of audits necessary to implement OMB A-133 audit requirements. (Welf. & Inst. Code § 11466.21.) The implementation of fraud and/or misuse audits are not "necessary" to implement OMB A-133 financial audits. Further, when a certified public accountant performs a financial audit, he or she will audit to the applicable government auditing standards, which are already contained in Chapter 4, Field Work Standards for Financial Audits. A copy of Chapter 4 is attached hereto as Exhibit 1.

"For example, Chapter 4 specifically defines the auditor's responsibility to design the audit to provide reasonable assurance of depicting material misstatements resulting from direct and material illegal acts. Field Work Standards then defines direct and material illegal acts "violations of laws and regulations having a direct and material effect on the determination of financial statement amounts." Essentially, the Field Work Standards employ accounting rules, which certified public accountants conducting such audits normally employ. The definition of "fraud and/or misuse" is an entirely different standard, and is but one aspect of so-called irregularities, illegal acts, or other types of non-compliance.

"The Alliance respectfully suggests that the definition of fraud and/or misuse should be deleted. Not only does it violate the Office of Administrative Law standard for necessity, it undoubtedly will create great ambiguity regarding the performance of audits. Thus, it would violate the clarity requirement of the Administrative Procedure Act.

"We also note that the original regulatory package noticed November 30, 2001, contained no definitions of fraud or misuse, and the inclusion of fraud and/or misuse definitions in the 15-day re-notice is not "sufficiently related" to the originally noticed provisions to properly employ a 15-day re-notice provision. When a regulatory change is not deemed "sufficiently related," a 45-day re-notice is required. (*State Water Resources Control Bd. v. Office of Admin. Law* (1993) 12 Cal.App.4th 697, 705.)

"While the Alliance objects to the inclusion of the definitions of fraud and misuse because they transcend the necessity and clarity standards, if the Department decides to retain the definitions, we strongly support the inclusion of the materiality provisions in the standard. In fact, they could be

substantially improved by employing the definitions in Chapter 4 of the Field Work Standards for Financial Audits in the Comptroller's Government Auditing Standards. That is, they would either have a direct and material effect on the determination of financial statement amounts or a material but indirect effect on the financial statements." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department disagrees with the comment that the phrase "by the Department" is necessary since the distinction regarding who conducts the fiscal audit is already contained in Section 11-405.11 and reinsertion of this phrase would be unnecessarily duplicative.

The Department also disagrees with the comment that the definition of fraud and/or misuse is unnecessary and not related to the originally noticed provisions and as such should be deleted. The OMB Circular A-133 standards require the Department's evaluation of the provider's financial audit through a management decision process, which includes notifying the provider of the action expected of the corporation to repay disallowed costs. Since misused and fraudulently expended AFDC-FC funds would equate to disallowed costs, there is a need to identify situations or actions which constitute misuse or fraud so that the Department can recover these funds.

6. Section 11-400f.(13)

Comment:

"Within the definition of Fraud in Section 11-400f.(13) an improper act must result in "material misstatements to the non-profit corporations financial statements." Also, fraud is stated as including "material misrepresentation, which results in the illegal expenditure of funds". There is no definition of the term "material" in the regulations nor is there guidance on how materiality will be determined, rendering the regulations governing fraud nearly unenforceable. Further, materiality has no relevance to a fraudulent act. If a provider commits fraud, the government cannot sanction that act up to a certain amount of money. Additionally, materiality is a relative term, therefore larger organizations could commit larger acts of fraud or misuse that might fall below the threshold of materiality and would not qualify as an act of fraud or misuse under the regulations. Thus, large organizations may not have committed fraud if the amount in question is only $100,000, while small organizations may be found to have committed fraud if the amount in question is $10,000. For these reasons, we object to acts of fraud being based on materiality and would like references to materiality removed from the regulations. Thus "…resulting in material misstatements to the non-profit corporation's financial statements." Should be deleted from the second

sentence of Section 11-400f.(13) and the word "material" should be struck from the third sentence of Section 11-400f.(13)." (Los Angeles)

Response:

The Department thanks the testifier for their comments. The Department disagrees with the testifier's recommendation to remove reference to materiality from the definition of "fraud." The definition of fraud is based on commonly accepted legal elements that comprise fraud and the Statement on Auditing Standards (SAS), Section AU 316, issued by the American Institute of Certified Public Accountants (AICPA). This AICPA reference provides a description and characteristics of fraud, which includes reference to "fraudulent acts that cause a material misstatement of financial statements." In addition, SAS Section AU 312.10 refers to Financial Accounting Standards Board Statement of Financial Accounting Concepts No. 2, which addresses the qualitative and quantitative aspects of judging materiality and defines materiality as "the magnitude of an omission or misstatement of accounting that, in the light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or misstatement." The assumption is that the omission or inclusion of immaterial facts is not likely to change or influence the decision of a rational external user. However, the materiality threshold does not mean that small items and amounts do not have to be accounted for or reported. For example, fraud is an important event regardless of the size or amount since it involves the intentional misrepresentation or concealment of information. Among the considerations that may well render material a quantitatively small misstatement of a financial statement item are whether the misstatement has the effect of increasing management's compensation, whether the misstatement affects the provider's compliance with regulatory requirements, and whether the misstatement involves concealment of an unlawful act.

7. Section 11-400m.(4)

Comment:

"Within the definition of "Misuse" in Section 11-400m.(4), unauthorized acquisition, use or disposition of assets for the personal benefit of any individual or individuals is limited to an act "that has a material effect on the financial statements." There is no definition of the term "material" in the regulations nor is there guidance on how materiality will be determined, rendering the regulations governing misuse nearly unenforceable. Further, materiality has no relevance to a misappropriation of assets for personal benefit. If a provider misappropriates assets, the government cannot sanction that act up to a certain amount of money. Additionally, materiality is a relative term, therefore larger organizations could commit larger acts of

misappropriation or misuse that might fall below the threshold of materiality and would not qualify as an act of misuse under the regulations. Thus, large organizations may not have misused assets if the mount in question is only $100,000, while small organizations may be found to have misused assets if the amount in question is $10,000. Further, use of the term "the financial statements" is not clear. Is the test of materiality limited to the particular licensee's financial statement for the year in question, or does it have to be material to all California licensees' financial statements? For these reasons, we object to misuse being limited to those that have a material effect of the financial statements and request that references to materiality be removed from the regulations. Thus, the words "…that has a material effect on the financial statements" should be deleted from the first sentence of Section 11-400m.(5)." (Los Angeles)

Response:

The Department thanks the testifier for their comments. The Department disagrees with the testifier's recommendation to remove reference to materiality from the definition of "misuse". The definition of "misuse" is derived from *Government Auditing Standards* (Yellow Book), Sections 4.25 and 4.26 which refer to the material effect on the financial statements. In comparison to "fraud," "misuse" as defined in the regulations, applies to acts that result in unintentional misstatements to the non-profit corporation's financial statements. The Statement on Auditing Standards (SAS), Section AU 312.10, issued by the American Institute of Certified Public Accountants (AICPA) refers to Financial Accounting Standards Board Statement of Financial Accounting Concepts No. 2, which addresses the qualitative and quantitative aspects of judging materiality and defines materiality as "the magnitude of an omission or misstatement of accounting that, in the light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or misstatement." The assumption is that the omission or inclusion of immaterial facts is not likely to change or influence the decision of a rational external user. However, the materiality threshold does not mean that small items and amounts do not have to be accounted for or reported. Among the considerations that may well render material a quantitatively small misstatement of a financial statement item are whether the misstatement has the effect of increasing management's compensation, whether the misstatement affects the provider's compliance with regulatory requirements, and whether the misstatement involves concealment of an unlawful act. The applicable financial statements for a financial audit submitted by the provider as a condition for receiving a rate are those that are associated with the provider's fiscal year in question. The financial statements in question for fiscal audits described in Section 11-405.11 may apply to any period in which the provider received AFDC-FC funds.

8. Section 11-402.222

Comment:

"This change is completely unrelated to the implementation of OMB A-133 audits. The section amended deals with the way social work points are counted and how social work weighting factors are employed. It is a rate issue and/or a program audit issue. Because this issue is unrelated to the implementation of AMB A-133 audits, there has been, at least to the Alliance's knowledge, no discussion with the Department regarding the propriety of the change. Further, it appears to the Alliance that social work activities (as opposed to the definition of a social worker to which a weighting factor applies) can and should be performed by persons who are not entitled to the "social worker" definition weighting factors. For example, a college graduate with a bachelor's degree in social work, but without the requisite two years' experience, is certainly qualified to perform certain social work activities as they are defined in the regulations (such as case management services). This change would not allow group homes and foster family agencies to utilize appropriately qualified people to engage in pointable social work activities.

"Further, a technical definition of a "social worker" only has application to weighting factors and, by implication, persons who are not qualified to utilize weighting factors will have their time completely eliminated as a result of this definitional change.

"It is not necessary to implement such a change as part of the OMB A-133 audit process, nor is it "sufficiently related" for purposes of Government Code section 11346.8(c) to be part of a 15-day re-notice provision. In short, if the Department wishes to adopt such a change, it could separately notice a different regulatory package and allow interested parties such as the Alliance to comment regarding the propriety of the proposed change." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department appreciates the time and effort that stakeholders have devoted to providing input into the development of these regulations. The Department acknowledges that this change is unrelated to the implementation of OMB Circular A-133 and has stricken this amendment from the regulation package.

Section 11-402.636

9. Comment:

"Concerning Section 11-402.636, it is not clear to us whether this paragraph would preclude the County from collecting on amounts questioned during one of our audits. Based on the wording in this paragraph it sounds as if the State would allow collection on a Fiscal Audit, or a Program Audit (whichever had the greater overpayment). If the State considers our audits to be Fiscal Audits, clearly we could be barred from collecting unallowed costs should a Program Audit also be performed on the agency in question. This we would not oppose. We would oppose any regulation that would otherwise preclude us from recovering unallowed costs. If the State does not consider our audits to be Fiscal Audits, the regulations do not appear to address the collection of unallowed costs and we prefer text that would clearly give us the right to do so. In addition, to fully implement Section 11-402.636, Section 11-402.643g. should be amended to add reference to the new Section 11-404." (Los Angeles)

Response:

The Department thanks the testifier for their comments. The Single Audit Act provides that "[A]n audit conducted in accordance with this chapter shall be in lieu of a financial audit of Federal Awards which a non-Federal entity is required to undergo under any other Federal law or regulation." One of the clear purposes of Congress in enacting this law was that the single audit would avoid duplication of effort, and that the subject matter embraced by the single audit precludes the performance of other audits covering similar subject matter. Therefore, a county should not perform a fiscal audit pursuant to Section 11-405.11 without specific written delegation by the Department. However, it was not intended to preclude other audits. Federal law at 31 USC 7502(f)(2)(B) provides that each pass through agency shall "monitor the subrecipient's use of Federal awards through site visits, limited scope audits, or other means." Moreover, it is the position of the Department that the Single Audit Act would not preclude a non-profit corporation operating a group home or FFA from entering into otherwise enforceable contract or other agreement with counties in relation to the placement of children that contain provisions that provide for the conduct of audits, and/or which permit recovery of funds under specified conditions. Such provisions however, would be in addition to the requirements set forth in these regulations, and would not impair or impact the authorities granted to the Department by these regulations.

Section 11-402.8

10. Comment:

"The Alliance is supportive of the changes to this section in the latest draft of the re-noticed regulations. This essentially confirms the Alliance's understanding that the pre-existing references to 45 CFR, Part 74, and 45 CFR, Part 1356, deal with reporting allowable costs, not expenditures of allowable costs. We note that the proposed regulatory package contains the same change in section 11-403(c)(1) for foster family agencies. The Alliance is supportive of both of the re-noticed provisions." (Alliance)

Response:

The Department thanks the testifier for their supportive comments and appreciates their time and effort devoted to providing input into development of these regulations.

Section 11-402.82

11. Comment:

"Concerning the deleted text in Section 11-402.82 and reliance on Internal Revenue Code Section 4958, we have found the guidelines for setting compensation levels for executive managers to be very helpful in our audits of Group Homes. No such guidelines exist for Foster Family Agencies and the lack of guidelines in this area has created frequent problems in determining what level of compensation is adequate for the Executive Director of an FFA, for example. We would encourage the State to retain specific guidelines for both Group Homes and Foster Family Agencies." (Los Angeles)

Response:

The Department thanks the testifier for their comments. The current regulations provided standards for executive salaries that were based on the Los Angeles Area United Way guidelines for Fiscal Year 1987-88. Given that the Los Angeles Area United Way has not updated the reasonable standards since 1987 and will not be updating the standards to reflect current market salaries, the Department believes that the Internal Revenue Code employed by the Department of Treasury's Internal Revenue Service is the appropriate authority to cite. This applies to non-profit corporations operating group homes and/or foster family agencies.

Section 11-402.828(c)

12. Comment:

"The Alliance is supportive of its understanding that the Department was going to reference Internal Revenue Code executive compensation standards so there was consistency between the tax standards which apply to nonprofits and the reasonableness standards for executive compensation for purposes of the AFDC-FC program. Unfortunately, we believe that the drafting of the provision does not accomplish the intended purpose. Internal Revenue Code (IRC) section 4958 imposes a tax on "excess benefit transactions." There are statutory definitions of "excess benefit transactions" in IRC section 4958. The problem with the drafting is that the proposed rule indicates that if compensation is provided "in accordance with Internal Revenue Code section 4958…" then it is deemed reasonable for purposes of reporting the AFDC-FC costs. Read literally, if the Internal Revenue Code imposes an excess benefit tax in compliance with section 4958, then the cost is deemed reasonable for AFDC-FC reporting purposes. The regulations should state the reverse if there is no excess benefit tax imposed pursuant to IRC section 4958, then the compensation shall be deemed reasonable for purposes of reporting AFDC-FC costs.

"The Alliance recommended the language employed in the proposed regulation. To the extent that the Alliance contributed to this problem, we apologize. The intention was to draft a provision which created consistency between the Internal Revenue Code Provision and AFDC-FC cost reporting standards.

"There is a similar provision in section 11-403(c)(1)(A)4. relating to foster family agency executive compensation, and the same comments apply." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department's specific purpose for this change is to provide that reasonable executive compensation is an allowable cost. The standard the Department shall use for determining what is reasonable executive compensation will be the standard employed by the Internal Revenue Service (IRS) for determining an "excess benefit transaction" as provided for in Internal Revenue Code Section 4958. If executive compensation constitutes an "excess benefit transaction" under these IRS rules, then it would be unreasonable and would thereby be an unallowable cost. The Department believes that the language found in Section 11-402.828(c) authorizes the Department to apply this IRS regulation in this manner.

Section 11-404

13. Comment:

"All foster care payments to both group homes and foster family agencies are a combination of federal, state and county dollars. The 11-404 provision, by its terms, references only the federal and state funds portion of a foster care payment. In order to enhance the clarity of the provision, either the reference to "Federal, State and County… ." Otherwise, the regulations imply a different use of funds policy for the federal and state share, and an undefined policy for the county share. We would urge the Department to be explicit in applying the policy to all AFDC-FC program funds. The adoption of explicit language will avoid a substantial "clarity" problem.

"Section 11-404.3 contains a definition of "foster care children." Because the definition limits foster care children placed in out-of-home care by a California "child welfare services or probation placement agency," the definition apparently excludes children placed by an "interagency placement committee." Welfare and Institutions Code section 11462.01, which defines the placement criteria for RCL 13 and RCL 14 children, requires those children to be placed by an "interagency placement committee." We urge the Department to add the phrase "interagency placement committee" to the placement criteria by "child welfare services" and "probation placement agency."

"Additionally, the regulatory definition appears to exclude children placed in out-of-home care pursuant to an individualized education program or IEP. Since such children are funded using the AFDC-FC funding stream, it would appear appropriate to include expenditures for their benefit in the out years. Thus, we have in the definition below included a reference to children placed pursuant to an IEP.

"Further, the definition of "foster care children" in section11-404.3 creates potential ambiguities in that the term "foster care children" is defined in terms of any "foster care child or youth." The definition that defines foster care children to include foster care children, we submit, is significantly ambiguous. We recommend the deletion of "foster care" at the end of the first line so that the definition would read:

> "For purposes of this section, the term 'foster care children' shall include any child or youth who is or has been placed in out-of-home care by a California child welfare services, interagency placement committee, probation placement agency, or pursuant to an individualized education program, including children who are placed out-of-state

pursuant to the Interstate Compact on the Placement of Children.

"We respectfully submit that the above language would eliminate the lack of clarity inherent in the definition of "foster care children" by reference to "foster care child or youth.

"The suggestion would also eliminate ambiguity regarding the relationship between the definition and the adjudicative process in the juvenile courts. Under current law, a detention hearing, at the beginning of the juvenile court process, triggers the availability of foster care resources to children. Without the suggested deletion, the definition could be construed to mean that a foster care child is not eligible for foster care services until the conclusion of the juvenile court adjudicative process." (Alliance)

Response:

The Department thanks the testifier for their comments. The Welfare and Institutions Code Section 15200 et seq. establishes the State/County share of costs in the State/federal foster care program. It is implicit in the statement "Federal and State AFDC-FC program funds, that these funds include county funds pursuant to Section 15200 et seq. Further, with respect to county-only funds, the Department has no authority to provide oversight for the expenditure of county-only funds. Accordingly, the Department does not believe specifying "county dollars" is necessary.

The Department respectfully disagrees with the testifier's comment on Section 11-404.3 that it excludes the placement of a foster care child through an interagency placement committee. The Welfare and Institutions Code Section 4096(c) states that the interagency placement committee membership includes "…at least the county placement agency…" Further, the interagency placement committee establishes procedures for "…a ward of the court or dependent child of the court…" [Welfare and Institutions Code Section 4096(e)]. As such, the placement of a foster care child through an interagency placement committee would meet this definition and therefore, would be eligible for activities under this section.

The Department also respectfully disagrees with the testifier's comment that children with an Individualized Education Plan (IEP) are precluded from receiving activities under this section. Existing statutory authority (Welfare and Institutions Code Section 18355) mandates the Department to fund out-of-home care for seriously emotionally disturbed children who are placed pursuant to an IEP in accordance with Section 7572.5 of the Government Code.

The Department respectfully disagrees with the testifier's comment that under the definition of foster care children that it could be construed that a foster child would be eligible for services until after the adjudication process. The Department contends that the detention hearing is the threshold event whereby all requisite findings are made in order to capture financial reimbursement. Therefore, regardless of the subsequent jurisdictional and dispositional hearings, the foster care child remains eligible for maintenance services, unless dependency is dismissed at one of these hearings.

Section 11-404.23

14. Comment:

"Section 11-404.23 indicates that the costs to start new programs, etc. shall be considered expended when received, provided that the majority of the population to be served by the program shall be California foster care children. It is unclear to us why we would be serving anyone other than California foster care children with Foster Care funds, so why would the reference to "majority of the population" be necessary? We advocate removal of the words "the majority of" from Section 11-404.23." (Los Angeles)

Response:

The Department thanks the testifier for their comments. Pursuant to Welfare and Institutions Code Section 11460 et. seq., AFDC-FC funds paid to foster care providers are earmarked for the care and supervision of California foster care children. It is the position of the Department while a foster care provider who has provided services commensurate with its rate for a fiscal year may in rare cases, have excess funds after that period, the purposes for which those public funds were paid, remain the same. At the same time, foster care providers may utilize these excess funds in many different ways that benefit California foster care children. To ensure that foster care providers enjoy maximum flexibility to perform such activities, and to foster an innovative environment where foster care providers can identify and address foster children's needs, it is important that the limitations imposed on the use of these funds not be excessively restrictive. Moreover, were the Department to apply a strict standard that only those programs or activities that exclusively benefit foster care children can be supported with these funds, foster care providers would be subject to undue risk from misapplying these funds, and would serve as a disincentive to creative program development. Accordingly, the Department has in Section 11-404.23 struck an appropriate balance by ensuring that foster care children are the primary beneficiaries of excess funds, while allowing foster care providers reasonable leeway in determining how they choose to utilize these funds.

Section 11-405.11

15. Comment:

"We previously suggested that the word "agents" is unclear, and we recommended that it be replaced by the word "designee." That language change would make the section "consistent" with the provisions of federal law in 42 U.S.C. section 671, which requires the state to perform audits, and Welfare and Institutions Code section 11466.2, which says the Department shall "perform or have performed" such audits. Absent an express delegation, there would be no "agent" if the Department accepted this recommendation." (Alliance)

Response:

The Department thanks the testifier for their comments. Because any person or entity designated by the Department to conduct fiscal audits on its behalf would necessarily become agents of the Department for that limited purpose, changing the relational description from "agent" to "designee" is not necessary.

16. Comment:

"Section 11-405.1.11 should be modified to allow fiscal audits that may be conducted by Counties pursuant to their contracts with Foster Care providers." (Los Angeles)

Response:

The Department thanks the testifier for their comments. The fiscal audits described in Sections 11-400f.(7) and 1-405.11 are distinct from audits the county may otherwise conduct. Any audits performed by the county pursuant to Sections 11-400f.(7) and 11-405.11 would be pursuant to specific written delegation by the Department. Section 11-405.24 clarifies that independent county audit activity that arises out of and conforms to the terms of contracts or placement agreements with such providers is not precluded by these regulations. Refer to response to Comment 9 for additional information on county authority associated with audits that are not in conflict with the Single Audit Act.

Section 11-405.213(a)(1)

17. Comment:

"This section lacks clarity if it is not limited to the determination of the $300,000 annual limit, which triggers the application of an A-133 audit. We suspect that the Department intends it to imply to the $300,000 limit, and suggest it be redrafted to read:

> "In determining whether a nonprofit corporation expends $300,000 or more in combined federal funds, federal foster care funds shall be deemed expended when received by the nonprofit corporation.

"As currently drafted, the section refer to all of section 11-405. During the performance of an OMB A-133 audit, funds should not be deemed expended until they are, in fact, actually expended pursuant to the applicable rules of accounting employed in the audit. Also, if an immediate expenditure rule applies to the performance of an OMB A-133 audit, a group home or foster family agency would be required to separately account for the federal portion, and the state and county portion which would be expended according to the normal rules of accounting. We hope the Department did not intend that result." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department disagrees that this section lacks clarity since it is a subsection of Section 11-405.21(a), which is limited to the determination of the $300,000 funding threshold. This section does not refer to all of Section 11-405.

18. Comment:

"Section 11-405.213(a)1. states that "For purposes of this section, federal Foster Care funds shall be deemed expended when received by the non-profit corporation". This section is discussed in the context of A-133 audits. Our question is what is the purpose of the A-133 audits if guidelines specify that receipt of the funds constitutes expenditure of the funds. There is no discussion on the need to expend the funds on reasonable and allowable items." (Los Angeles)

Response:

The Department thanks the testifier for their comments. Section 11-405.213(a)(1) was proposed for the sole and limited purpose of administrative convenience in the identification of those non-profit

corporations operating a group home or FFA that are subject to the OMB Circular A-133 audit requirement. Without this provision, it will be necessary to track expenditures for the purpose of determining whether or not the monetary threshold for application of OMB Circular A-133 standards is reached for each non-profit corporation operating a group home or FFA. To avoid this unduly administratively burdensome process, the Department has opted to determine whether or not the monetary threshold for application of OMB Circular A-133 standards is reached through a far more administratively convenient process of determining the amount of federal funds a non-profit corporation operating a group home or FFA received in a fiscal year. In addition, the Department of Health and Human Services, Administration for Children and Families has determined that payments to providers under California's capitated rate structure are considered expended when the rate is paid. In response to the comment that there is no discussion on appropriate expenditure of funds, Section 11-404 already addresses the use of Federal and State foster care funds and requires that AFDC-FC program funds be used to meet the cost of providing care and supervision for AFDC-FC eligible children. Therefore, such reference is not necessary in this section.

Section 11-405.231(a)

19. Comment:

"The Alliance previously commented in January 2002 (sic) that management decisions are made either by the cognizant federal agency or the pass-through entity. In California, the pass-through entity would be the county. In order to be consistent with both federal and state law, which concentrates the audit function in the state, the Alliance supports the regulatory requirement that the Department issue management decisions on audit findings." (Alliance)

Response:

The Department thanks the testifier for their supportive comments and appreciates their time and effort devoted to providing input into the development of these regulations.

Sections 11-405.231(b) and (c)

20. Comment:

"Under OMB A-133, the management decision process is the governmental review of annual financial audits performed by certified public accountants. Subdivisions (b) and (c) also apply management decision review to fiscal audits and fraud and/or misuse audits. California's statutes (Welf. & Inst. Code §§ 11463.5, 11466.2, 11468.6.) and the Department's rate regulations

have historically contained administrative review procedures for program and fiscal audits. We submit the existing regulations in MPP 11-430 et seq. are the appropriate administrative procedures to review fiscal audits and/or fraud and/or misuse audits.

"The proposed regulations essentially create different and conflicting review procedures for fiscal audits and fraud and/or misuse audits. For fiscal audits and fraud and/or misuse audits, the Department should use the two-step administrative review process that is currently in the 11-430 series of these regulations. The management decision review under 11-405.232 is a single level of review which eliminates the entire informal level of administrative review. Welfare and Institutions Code section 11468.6 still mandates a two-level administrative review process when the Department seeks to collect an overpayment from a group home. That mandate would apply to fiscal audits and/or fraud or misuse audits that seek to recover an overpayment.

"Welfare and Institutions Code section 11466.2 in subdivision (c) specifically requires a consistent set of standards, rules and auditing protocols. It is submitted that the management decision process, with its different set of review standards than those contained in the 11-430 series, will not comply with either Welfare and Institutions Code sections 11466.2 or 11468.6. Succinctly stated, the consistency requirement of the Administrative Procedure Act could also be violated in that the proposed standards are not consistent with the authorizing statutory provisions cited.

"We also note that the implementation of administrative review procedures for fiscal audits and fraud and/or misuse audits are not "sufficiently related" to the implementation of OMB A-133 audits as to satisfy the requirements of Government Code section 11346.8(c)." (Alliance)

Response:

The Department thanks the testifier for their comments and appreciates their time and effort devoted to providing input into the development of these regulations. The Department intends to use a consistent process for evaluating financial information from financial audits and fiscal audits and issuing management decisions on audit findings, including any action expected of the corporation. Any management decision which addresses recoupment of funds from the provider will be based on a review of the audit findings, any responses from a non-profit corporation to the findings, and findings from any additional audits conducted by the Department or its designee.

The major difference in the administrative review process set forth in the proposed regulations and the administrative review process advocated by the testifier is that in the latter, an informal hearing is required along with a

formal hearing. The Department believes that providing for an informal hearing in the management decision process is redundant, inefficient, and will result in increased costs for all parties to a disputed management decision. It is redundant in part because a group home or FFA provider who objects to one or more deficiencies identified in the audit report will have an opportunity under OMB Circular A-133 standards to present those objections to the Department along with the submission of the provider's response to the Department's audit findings. In preparing the Department's management decision on recoupment, Departmental staff will have an opportunity to consider those objections. To require or allow an informal hearing under these circumstances will result in the Department having to reconsider issues it already considered at the point it prepared the management decision. This would result in inefficiencies and undue administrative costs in the management decision process. The formal administrative review process set forth in the regulations is modeled after the administrative review process established by the Legislature for review of provisional rate audits. The Department has significant experience with this process, and has determined that it is an efficient and effective administrative review process that will afford ample due process to providers who object to the Department's management decision.

Since financial audits and fiscal audits are both associated with the review of financial information, use of the management decision process for these audits would be appropriate and consistent. Using the management decision process for financial audits and a different review process for fiscal audits to address financial matters would result in inconsistent application of standards. Furthermore, use of the current informal administrative review procedures contained in Section 11-430, which address audit findings associated with Rate Classification Levels and adjustments to a group home provider or foster family agency's rate, for fiscal audits is inappropriate.

Since OMB Circular A-133 standards require that the Department monitor the activities of providers as necessary to ensure that Federal awards are used for authorized purposes, the Department has a responsibility to question information provided in a financial audit report if there is a reason to do so. Accordingly, a fiscal audit may be initiated as a result of the Department's review of a financial audit report submitted by a group home or foster family agency provider. As such, there is a need to establish a management decision process which includes an appeal process for fiscal audits as well as for financial audits.

Section 11-405.232

21. Comment:

"This section contains the administrative review procedure following a management decision. Given the fact that the management decision may differ substantially from the findings or opinions of the certified public accountant-performed audit, we submit that the 30-day review time is too short, given the requirements for simultaneously providing all supporting documentation. After an audit is performed by a certified public accountant, the Department has six months to issue its management decision. Then the provider has 30 days to contest the management decision and provide all supporting documentation. That simply is not sufficient time for the nonprofit to prepare its request for review. We note that for the two-level administrative review process in MPP section 11-430, the provider has 60 days to appeal after the informal process is completed." (Alliance)

Response:

The Department thanks the testifier for their comments and appreciates their time and effort devoted to providing input into the development of these regulations. Since the Department will not issue a management decision regarding its decision on recoupment until a provider has been given an opportunity to respond to the Department's audit findings, the provider will have already been given time to obtain and provide supporting documentation. Documentation pertaining to issues associated with the Department's audit findings should be readily available in the event the provider decides to appeal the Department's management decision. Accordingly, allowing 30 days for the provider to file a hearing and include all supporting documentation after the Department issues the management decision is sufficient. In addition, Section 11-430.511, which will apply to the hearing process, allows for an extension of time to provide additional documentation if good cause is justified.

Section 11-405.24

22. Comment:

"This section indicates there is nothing in the 11-405 series which precludes counties from conducting site visits or from performing "audits" to verify compliance with the terms of any contract or agreement between a county placement agency and a group home and/or foster family agency. The Alliance has multiple concerns with this provision. First, it has nothing to do with implementing OMB A-133 audits. County "audits," pursuant to the terms of county contractual provisions, are simply unrelated or in the statutory language not "sufficiently related" to the original noticed

regulations to be included in this regulatory package without employment of a 45-day re-notice.

"Substantively, it raises serious issues regarding the "consistency" and "authority" regarding the state's implementing legislation. It is clear, under Welfare and Institutions Code sections 11466.2, 11466.22 and 11463.5, that the state is the agency which is to perform program, fiscal, and other audits. Further, it is also clear pursuant to the authorizing statutes and the Department's regulations in the 11-405 series, that certified public accountants perform OMB A-133 audits. This section authorizes counties, by contract, to audit to their own unique contractual standards. Given the fact that there are 58 counties in the state, and many providers receive placements from numerous counties, we submit that this provision violates the mandates of the federal law for a unified administrative and regulatory oversight system. (42 U.S.C. § 671.) As well, it violates the provisions in the Welfare and Institutions Code, which require a consistent set of auditing protocols and standards. This is an invitation for counties to create 58 different sets of rules, which would not, we submit, comply with either federal or state statutes.

"In order to remedy this inconsistency with the authorizing statutes, the Department should either delete this section in its entirely or it should require that county auditing standards and auditing protocols be consistent with both federal and state law, and not duplicate any audits performed by state agencies or certified public accountants, whether characterized as program audits, fiscal audits, financial audits, or fraud and/or misuse audits. The problem is not merely theoretical; the current Los Angeles County contract for foster family agencies purports to limit foster family agency expenditures to OMB A-122 standards. Under the Department's regulatory package, that is a cost reporting issue, not an overpayment issue. The Alliance prefers this section be deleted." (Alliance)

Response:

The Department thanks the testifier for their comments. The Department believes that this section is necessary to clarify the authority of the county to conduct audits in light of application of OMB Circular A-133 standards, and application of the Federal Single Audit Act at 31 USC 7503. The Single Audit Act provides that "[A]n audit conducted in accordance with this chapter shall be in lieu of a financial audit of Federal Awards which a non-Federal entity is required to undergo under any other Federal law or regulation." One of the clear purposes of Congress in enacting this law was that the single audit would avoid duplication of effort, and that the subject matter embraced by the single audit precludes the performance of other audits covering similar subject matter. However, it was not intended to preclude other audits. Federal law at 31 USC 7502(f)(2)(B) provides that

each pass through agency shall "monitor the subrecipient's use of Federal awards through site visits, limited scope audits, or other means." Section 11-405.24 is necessary to delineate the type of County audit activity that is not precluded by application of OMB Circular A-133 standards.

23. Comment:

"In the first sentence of Section 11-405.24, please change the words "this section" to Chapter 11-400". Further, we object to the last sentence of this paragraph "Such activities shall not duplicate audits conducted in accordance with OMB Circular A-133." We believe that this could place broad restrictions on what we would be able to audit as part of one of the County reviews provided for in this section. We do not oppose language that would prevent an agency from being subject to double jeopardy on collection of questioned costs, but this language is clearly intended to restrict the scope of a County initiated audit. The inclusion of this language also creates confusion, as its effect is subject to interpretation. Thus the last sentence in Section 11-405.24 should be deleted.

"In conclusion, we appreciate the inclusion of Section 11-405.24 in these regulations. We hope that you will not delete Section 11-405.24 (other than the last sentence) in subsequent rewrites. We further appreciate any changes you may be able to make as outlined above supporting the counties' ability to audit for and collect unallowed costs and ensuring the State's own ability to effectively audit for and collect unallowed costs." (Los Angeles)

Response:

The Department thanks the testifier for their comments. The last sentence in Section 11-405.24 clarifies that any audit activity conducted by a county pursuant to its placement contract or agreement with a non-profit corporation operating a group home and/or foster family agency shall not duplicate the OMB Circular A-133 audit. This provision is necessary to avoid potential inconsistent results from the conduct of the same audit activity by avoiding redundant audits and helps to ensure compliance with the Single Audit Act.

24. Comment:

"It is not clear to us from the regulations whether the audits that counties may conduct under Section 11-405.24 are considered separate and apart from the Fiscal Audits defined at paragraph 11-400f.(7), or whether the State considers our audits to be Fiscal Audits. It is our opinion that our audits may be construed to meet the definition of a Fiscal Audit as defined in Section 11-400f.(7) of the regulations. As Section 11-405.1 states that fiscal audits shall be performed by the Department, its agents, or an audit agency of the federal government and the language in Section 11-405.24 (discussed further below)

does not mention fiscal audits, the counties' right to audit and collect misappropriated funds pursuant to contract is subject to question. We oppose any regulation that precludes the counties from conducting fiscal audits." (Los Angeles)

Response:

The Department thanks the testifier for their comments. The fiscal audits described in Sections 11-400f.(7) and 11-405.11 are distinct from audits the county may otherwise conduct. Any audits performed by the county pursuant to Sections 11-400f.(7) and 11-405.11 would be pursuant to specific written delegation by the Department. Section 11-405.24 clarifies that independent county audit activity that arises out of and conforms to the terms of contracts or placement agreements with such providers is not precluded by these regulations.